

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1903

No. 224

CIVIL AERONAUTICS BOARD, PETITIONER,

ARTHUR M. SUMMERFIELD, POSTMASTER GENERAL OF THE UNITED STATES, THE UNITED STATES OF AMERICA, ON BEHALF OF THE POSTMASTER GENERAL AND WESTERN AIR LINES, INC.

No. 225

WESTERN AIR LINES, INC., PETITIONER,

CIVIL AERONAUTICS BOARD, ARTHUR M. SUMMERFIELD, POSTMASTER GENERAL OF THE UNITED STATES, AND THE UNITED STATES OF AMERICA, ON BEHALF OF THE POSTMASTER GENERAL.

ON WRIT OF HABEAS CORPUS TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

PRINTING FOR CHRISTIAN FELD JUL 12, 1904

CHRISTIAN GRAYED OCTOBER 12, 1904

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JOINT APPENDIX

Filed Dec 10 1951

IN THE

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT.

No. 11259

JESSE M. DONALDSON, Postmaster General of the United States, and THE UNITED STATES OF AMERICA, on Behalf of the Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

Petition for Judicial Review

To the Honorable, the Judges of the United States Court of Appeals for the District of Columbia Circuit:

Jesse M. Donaldson, Postmaster General of the United States, and The United States of America, on Behalf of the Postmaster General, petitioners, by their attorneys, respectfully present this petition for judicial review of orders of respondent, Civil Aeronautics Board, and in support thereof represent and allege the following:

THE STATUTES AND THE FACTS UPON WHICH JURISDICTION IS
BASED

(1) This petition for judicial review of the Board's orders is filed pursuant to provisions of Section 1006 of the Civil Aeronautics Act, 52 Stat. 1024 (1938), 49 U.S.C. § 646.

(2) This petition seeks review of two mail rate orders of the Civil Aeronautics Board issued in the Board's proceedings entitled *Inland Air Lines, Inc., and Western Air Lines, Inc., Mail Rate Proceeding*, Docket No. 2870 *et al.*, Order No. E-5467, dated June 26, 1951, and Order No. E-5782, dated October 12, 1951.

(3) The Board's proceedings were conducted under the provisions of the mail rate section (Sec. 406) of the Civil Aeronautics Act, 52 Stat. 998 (1938), 49 U.S.C. § 486.

(4) The Postmaster General, as head of the Post Office Department of the United States, is a statutory party in all mail rate proceedings before the Board, Section 406(a) and (c) of the Civil Aeronautics Act, *supra*, and has been judicially determined to be the protector of the public interest in air mail rate proceedings. *Seaboard & Western Air Lines v. Civil Aeronautics Board* (1949), 86 U.S. App. D.C. 64, 181 F. (2d) 515, 518-519, certiorari denied (1950) 339 U. S. 963. The Postmaster General participated in the particular mail rate proceeding out of which emerged the orders sought to be reviewed. The Postmaster General is required by the Act to pay, from appropriations for the transportation of mail by aircraft, the air mail rates fixed and determined by the Board, pursuant to the mail pay section of the Act, Section 406(a) of the Civil Aeronautics Act, *supra*. Accordingly, the Postmaster General has a substantial interest in said mail rate orders sought to be reviewed, within the meaning of the judicial review section of the Act, Section 1006 of the Civil Aeronautics Act, *supra*.

(5) This petition is filed within the statutory period of 60 days after entry of the Order of October 12, 1951, *supra*, which was the final order of the Board denying the Postmaster General's petition for reconsideration. Section 1006, Civil Aeronautics Act, *supra*.

II

THE NATURE AND FACTS OF THE PROCEEDINGS AS TO WHICH REVIEW IS SOUGHT

(1) The orders of the Board sought by the petitioners to be reviewed arose out of the mail rate proceeding for Western Air Lines, Inc. This rate proceeding was initiated under the mail pay section (406) of the Act, *supra*, upon petition filed by Western on April 26, 1944. The proceeding was later consolidated with the mail rate proceeding of Inland Air Lines, Inc., a subsidiary of Western.

(2) While Western's mail rate proceeding was pending, Western, in a totally distinct proceeding, obtained approval in 1947 from the Board to sell one of its route certificates, namely, Route 68 extending from Denver to Los Angeles, together with certain related operating equipment, for the lump sum of \$3,750,000. *United-Western Acquisition Air Carrier Property* (1947), 8 C.A.B. 298.

(3) Thereafter, as finally adopted by the Board in the orders to which this petition is directed, the Board fixed a final mail rate for Western for the past rate period, commencing April 26, 1944 and ending December 31, 1948. The rate so fixed was computed on the basis of a rate-making principle which the petitioners believe to be unlawful, and to which the Postmaster General objected in the proceedings before the Board. The opinion of the Board accompanying the Order of June 26, 1951, *supra*, although recognizing that the Board was fixing a "need" rate under the subsidy provisions of the mail rate section of the Act and that in fixing the rate the Board must "take into consider-

ation" the profits Western received under the said sale, as "other revenue," nevertheless ruled:

"While we are required by the Act to 'take into consideration' the 'need' of the carrier for mail compensation together with 'all other revenue', we do not understand the language of section 406(b) as requiring us to reduce the carrier's mail pay 'need' with any part of such 'other revenue.' This is a matter within our discretion. *That is, we may take in 'other revenue' in whole, in part, or not at all.*" Board's Order E-5467, June 26, 1951, Opinion, p. 5, *supra*. (Emphasis supplied.)

(4) Thereupon the Board proceeded to allocate the determined profit of \$1,099,000 obtained from the sales transaction into profit from the sale of tangibles and profit from the sale of intangibles. In determining the "need" of Western for mail compensation, that part of the profit attributable to the tangible elements of the sale, namely, the operating equipment, was taken into account, but the Board excluded from its computations the remaining \$447,000 assignable to the profit from the sale of the intangibles, namely, the route certificate.

(5) The administrative remedies of the Postmaster General before the Board are now exhausted.

III

POINTS RELIED ON

(1) The Board exceeded its statutory power or, in the alternative, abused its discretion in failing to apply the entire net profits from the said sales transaction in evaluating the carrier's subsidy "need."

(2) The mail rate section (406(b)) of the Act, *supra*, requires the Board to apply the entire net profit obtained by Western from the said sales transaction when determining the true "need" of the carrier for subsidy mail compensation.

(3) To the extent that the carrier has obtained "other revenue"—the entire net profit of the sale—from other sources during the rate period involved, the carrier has no subsidy "need" under the Act for additional compensation in the form of mail pay.

(4) The rate being fixed by the Board for Western is based on the subsidy "need" of the carrier under the unique subsidy feature of the Act; such rate is not a "service" rate. A service rate has been defined by the Board to be a rate intended to cover only those operating expenses of the carrier allocable to the mail services rendered by such carrier, together with a net profit sufficient to yield an adequate return only upon that part of the carrier's investment allocated to the mail service.

(5) When fixing a subsidy rate the Board is required under the Act to review and apply the financial results of the carrier in order to determine the true subsidy "need" in the light of all "other revenue" of the carrier; the Board has failed in its statutory duty to apply such "other revenue."

(6) The Board erred in splitting up the one-package sales transaction and in failing to apply as "other revenue" that portion of the net profit of such sales transaction attributable to the route certificate.

(7) The route certificate entitled the carrier to subsidy mail pay to cover its financial needs; upon the sale thereof by a going carrier, any profit accruing to such carrier should be applied against the carrier's "need" for subsidy; failure to apply such profit is contrary to the public interest and unlawful because nonapplication would result in the payment of additional public funds to subsidize a need already covered by profits accruing from the benefit of such certificate.

(8) A route certificate received by the carrier from the Government is a matter of free public grant. The Act specifically provides that, "No certificate shall confer any

proprietary, property, or exclusive right." Section 401(j) of the Civil Aeronautics Act, 52 Stat. 990 (1938), 49 U.S.C. § 481(j). The holder of a certificate holds it for the benefit of the public. Any value of the certificate belongs to the public. The public has made the sole contribution to the value placed upon the certificate. By the ruling challenged herein, the Board in effect has determined that the public must pay to Western, the seller, a premium for transferring a certificate in which Western has no property interest.

(9) Since the Board determined that the profit from the tangible elements of the sales transaction—the operating equipment in which the carrier had a vested interest—should be included as "other revenue," then by even greater force and reason the profits from the intangible elements of the sales transaction—the route certificate in which the carrier had no vested interest—should also be included and applied as "other revenue" against any claimed "need" of the carrier for subsidy.

(10) The Civil Aeronautics Board, as well as other regulatory bodies, has definitely ruled against the inclusion of franchise values in rate bases when fixing rates in other proceedings. The orders of the Board challenged by this petition not only recognize and place a net monetary value of \$447,000 on the said route certificate and find that Western actually made that profit, but also disregard that profit as "other revenue" with the result that Western can now collect from the public treasury an additional \$447,000 as subsidy in the form of mail pay.

(11) Nowhere in the Act is there any permission for carriers to traffic in air certificates for private gain. It is only in the public interest, as distinguished from the private interests, that certificates may be transferred. Section 401(i) of the Civil Aeronautics Act, 52 Stat. 989 (1938), 49 U.S.C. § 481(i).

(12) Failure by the Board to follow the stated policy of Congress set forth in the Act as the guidepost for the Board in fixing the proper mail rate subsidy, is not only detrimental to the public interest in this particular proceeding, but if permitted to go unchallenged may permit other carriers to ask the Board to ignore all sorts of revenues when fixing the subsidy "need" of such carriers. Unless it is judicially reviewed, the Board's ruling would permit, without any standard or limitation, the perpetuation in air mail rate proceedings of a principle that carriers have a "need" for subsidy where no such "need" actually exists.

IV

THE RELIEF PRAYED

WHEREFORE, The petitioners pray:

(1) That a copy of this petition be served upon the Civil Aeronautics Board;

(2) That said Board be required to certify and file in this Court a transcript of the records of the proceedings in which Orders Serial No. E-5467, dated June 26, 1951, and No. E-5782, dated October 12, 1951, of the Board, were entered, in accordance with the requirements of Section 1006 of the Civil Aeronautics Act, *supra*;

(3) That said orders of the Board be reviewed and declared unlawful as beyond the statutory power of the Board, or in the alternative, as constituting an abuse of discretion, and that the said orders be set aside or so modified as to reduce the mail pay awarded to Western by the appropriate amount to reflect the inclusion of all the profits from the sale of Route 68 in the computation of Western's needs; and

(4) That the petitioners be given such other, further, general, and different relief as the nature of the case may

require, and as the Court may deem just, proper, and appropriate.

Dated December 10, 1951.

(Signed) NEWELL A. CLAPP

Newell A. Clapp

*Acting Assistant Attorney
General*

*Department of Justice
Washington 25, D. C.*

(Signed) LOUIS J. DOYLE

Louis J. Doyle

Acting Solicitor

*Post Office Department
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Chief, Air Mail Section

Office of the Solicitor

Attorneys for Petitioners

Filed Feb. 23, 1952

IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

No. 13195

WESTERN AIR LINES, INC., *Petitioner*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

Petition of Western Air Lines for Review of Orders of the Civil Aeronautics Board

*To the Honorable Justices of the United States Court of
Appeals for the Ninth Circuit:*

Western Air Lines, Inc., Petitioner, (to be referred to as "Western") presents this petition for review of and to set aside orders of the Civil Aeronautics Board (to be referred to as the "Board"), dated December 30, 1948, Serial No. E-2333; dated November 24, 1950, Serial No. E-4870; dated June 26, 1951, Serial No. E-5467; and dated October 12, 1951, Serial No. E-5782.

I

BACKGROUND OF THE ORDERS UNDER REVIEW

Western is a commercial air carrier holding certificates of convenience and necessity issued by the Board pursuant to the Civil Aeronautics Act of 1938.

Section 406 of the Act (49 U. S. Code 486) vests in the Board the power to fix the rate of compensation to be paid to air carriers for the transportation of mail and sets forth the elements which should be considered by the Board in fixing the rate.

On April 26, 1944, Western filed a petition with the Board for an order increasing the compensation to be paid

to Western for the transportation of mail. Subsequently, five separate amendments to the petition were filed by Western.

Following acceptable procedures, on December 30, 1948, the Board issued its first order in the proceeding, which is designated as Serial No. E-2333, the effect of which was to decree that Western was entitled to additional compensation for the transportation of mail from May 1, 1944, through December 31, 1948, in the sum of \$975,000.00. Western noted its objections to this order in the manner permitted by the Act and by the rules and regulations of the Board.

Thereafter, following acceptable procedures, on November 24, 1950, the Board issued its order, Serial No. E-4870, the effect of which was to decree that Western had been overpaid for the transportation of mail between May 1, 1944, through December 31, 1948, by virtue of the order of December 30, 1948, Serial No. E-2333, in the sum of \$671,474.00. Western noted its objections to this order in the manner permitted by the Act and by the rules and regulations of the Board.

Thereafter, following acceptable procedures, on June 26, 1951, the Board issued its order, Serial No. E-5467, the effect of which was to decree that Western had been overpaid for the transportation of mail between May 1, 1944, through December 31, 1948, by virtue of the order of December 30, 1948, Serial No. E-2333, in the sum of \$342,973.00. In the manner permitted by the Act and by the rules and regulations of the Board, Western noted its objections in the form of a petition for reconsideration.

Thereafter, following acceptable procedures, on October 12, 1951, the Board issued its final order, Serial No. E-5782, the effect of which was to decree that Western had been overpaid for the transportation of mail between May 1, 1944, through December 31, 1948, by virtue of the order of December 30, 1948, Serial No. E-2333, in the sum of \$334,639.00, and otherwise denying a reconsideration.

Western's grievance is based on the inequities of the final order of October 12, 1951, but the relationship of the

three preceding orders to the final order makes it appropriate that this petition for review include the four orders in the proceeding which have been listed.

II

ISSUES FOR REVIEW

The issues to be resolved under this petition for review are:

1. Did the Board commit legal error in including as other revenue within the meaning of Section 406(b) of the Act (49 U. S. Code 486(b)) the profit derived by Western from the sale of its certificate of convenience and necessity for Route 68 and related equipment and the profit derived by Western from the operation of restaurants, concessions and coin machines as an element in fixing the compensation Western was entitled to receive for the transportation of mail?

2. Did the Board commit legal error in redetermining Western's mail pay compensation for the period from May 1, 1944, through December 31, 1948, instead of the period from January 1, 1946, through December 31, 1948?

3. Did the Board commit legal error by ordering the equivalent of a recapture of a portion of the compensation paid to Western for the transportation of mail from May 1, 1944, through December 31, 1945, which compensation was on a service or compensatory basis without subsidy?

4. Did the Board commit legal error in the method it adopted for calculating the allowance for Western's income tax as an element in fixing the compensation Western was entitled to receive for the transportation of mail?

III

COMMENTS ON ISSUES FOR REVIEW

Section 406(b) of the Act (49 U. S. Code 486(b)) requires the Board in fixing the mail rate of air carriers to consider:

" . . . the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

Issue 1 on this review seeks a judicial interpretation of the term "other revenue" as used in this section. Western took and still takes the position that the term "other revenue" necessarily means revenue derived by the carrier from its air transportation operations. It does not mean revenue derived from other sources. Otherwise, an air carrier fortunate enough to own land producing oil in goodly quantities would have sufficient other revenue to preclude the need for any compensation for the transportation of mail.

It is important to the air transportation industry to have a judicial interpretation of the term "other revenue" as used in Section 406(b) of the Act in order that air carriers may calculate with some degree of certainty the consequences on its mail compensation of engaging in activities wholly unrelated to air transportation and in activities which may be indirectly related to air transportation. It was Western's position before the Board and it will be Western's position before this Court that the profit it derived from the sale of its certificate of convenience and necessity for Route 68 and related equipment, as well as the profit it derived from the operation of restaurants and coin machines, should not be included as other revenue within the meaning of that term as used in Section 406(b) of the Act.

Issues 2 and 3, which are interrelated, concern the right of the Board to redetermine Western's mail compensation from May 1, 1944, the approximate date of the filing of Western's original petition for that purpose, notwithstanding the fact that:

(a) The original petition sought only an increase, not a decrease;

(b) Prior to any action being taken by the Board, Western disclaimed any desire to have its rate reconsidered back of January 1, 1946, and objected to considering any period back of that date;

(c) The effect of the order is to recapture compensation already paid under an effective order, thus constituting an ex post facto ruling; and that

(d) The effect of the order is to compel Western to refund a portion of mail pay based on a compensatory or service rate with no subsidy, and thereby to compel Western to carry the mail at less than a fair and reasonable rate, resulting in a taking of property rights without just compensation.

Issue 4 relates to the method the Board employed to calculate the allowance for Western's income taxes in determining the mail compensation to be allowed. The method used was different than the method used in the first order in this proceeding, dated December 30, 1948, Serial No. E-2333, and in effect amounted to an ex post facto ruling. The new method is cloaked with legal improprieties and injustices, and it was unjust and legally improper for the Board to adopt a new method and apply it retroactively.

The four issues involved in this petition for review are of great importance to Western and of major significance to the air transportation industry.

IV

BASIS FOR JURISDICTION

This petition is filed pursuant to Section 1006 of the Civil Aeronautics Act of 1938, 52 Stat. 973, 1024, 49 U.S.C. 401, 646, and Section 10 of the Administrative Procedure Act, 60 Stat. 237, 243; 5 U.S.C., 1001, 1009.

Section 1006 of the Civil Aeronautics Act provides in part that any order issued by the Board shall be subject

to review by the Circuit Court of Appeals for the Circuit wherein the petitioner resides or has its principal place of business or in the United States Court of Appeals for the District of Columbia.

The principal place of business of Petitioner is in Los Angeles, California.

V

RELIEF REQUESTED

Western requests relief under this petition for review in the form of an order of this Court:

1. Directing that the orders of the Board under review be set aside or modified in such manner as may be necessary to correct the legal errors committed by the Board;

2. Directing the Board to recalculate the compensation to be paid to Western for the transportation of mail during the appropriate period prior to December 31, 1948, in a manner which will eliminate the errors of law and the injustices appearing in the orders under review and in a manner which will provide Western with the fair and reasonable compensation contemplated by Section 406 of the Act; and

3. Awarding Western such other redress as the law and the record may justify.

Los Angeles, California.

December 7, 1951.

Respectfully submitted,

GUTHRIE, DARLING & SHATTUCK,
By HUGH W. DARLING,
737 Pacific Mutual Building,
Los Angeles 14, California,
*Attorneys for Western Air
Lines, Inc.*

Filed April 26, 1944

BEFORE THE
CIVIL AERONAUTICS AUTHORITY

No. 1374

In the Matter of the Petition
of

WESTERN AIR LINES, INC., for an order fixing the fair and reasonable rates of compensation for the transportation of air mail over Air Mail Routes 13, 19, 52 and 63.

Petition

TO THE HONORABLE, THE CIVIL AERONAUTICS BOARD:

1. The Petitioner is a corporation duly organized and existing under the laws of the State of Delaware, and has operated as a common carrier by air and is now operating, or is certificated to operate, over the following routes under certificates of convenience and necessity for the transportation of mail, passengers and property:

a. Route 13, between the terminal point San Diego, California, the intermediate points El Centro, Palm Springs, San Bernardino, Long Beach, Los Angeles (Burbank) California, and Las Vegas, Nevada, and the terminal point Salt Lake City, Utah. (Inauguration of service to El Centro, Palm Springs and San Bernardino has been deferred because of requirements of the National Defense).

b. Route 19, between the terminal point Salt Lake City, Utah, the intermediate points Ogden, Utah, Pocatello and Idaho Falls, Idaho, West Yellowstone, Butte and Helena, Montana, and the terminal point Great Falls, Montana. (Service has been temporarily suspended to Ogden, Utah, Idaho Falls, Idaho and West Yellowstone, Montana).

c. Route 52, between the terminal point Great Falls, Montana, the intermediate point Cut Bank-Shelby, Mon-

tana, and the terminal point Lethbridge, Alberta, Canada. (The Petitioner also is the holder of a franchise issued by the Dominion of Canada, authorizing its operation of Route 52).

d. Route 63, between the terminal point Los Angeles, California, and the terminal point San Francisco, California. (Services on this route will be inaugurated on May 1, 1944).

2. This petition is filed pursuant to the provisions of Section 406, among others, of the Civil Aeronautics Act of 1938, as amended.

3. On May 10, 1943, the Board amended Petitioner's certificate for Route 13 to include El Centro, Palm Springs and San Bernardino, California as intermediate points between San Diego, California and Long Beach, California. The amended certificate provides that service shall not be inaugurated to any of the new intermediate points until the Board shall have notified Petitioner that the National Defense no longer requires that the inauguration of
2 such service be delayed. Petitioner has received no such notice from the Board, and therefore, has no plans for immediate inauguration of service to these points. When sufficient equipment is available that service may be started, it is believed public convenience and necessity will require a minimum of two round trips daily to these intermediate points.

4. On August 13, 1943, the Board issued Petitioner a certificate to engage in air transportation with respect to persons, property and mail, between the terminal point Los Angeles, California and the terminal point San Francisco, California. This certificate carried a provision that the service should not be inaugurated until the Board notified the Petitioner that the National Defense no longer required that the inauguration of such service be delayed. Petitioner recently received such notice from the Board and will commence service on this route with three round trips daily effective May 1, 1944.

5. On November 8, 1943, the Civil Aeronautics Board issued an order fixing and determining the fair and reasonable rate of compensation for transportation of mail by aircraft, the facilities used and useful therefor, and the service connected therewith between the points between which Petitioner is authorized to carry mail by its certificates of public convenience and necessity. Such rate was determined to be 0.3 mill per pound mile of mail carried computed on direct airport to airport mileage, and was made retroactively effective as of January 1, 1943.

6. The present rate does not provide a fair and reasonable compensation for the Petitioner for its transportation of mail by aircraft, its facilities used and useful therefor and its service connected therewith between the points between which Petitioner is authorized to carry mail by its certificates of public convenience and necessity. The income derived therefrom together with all other revenues of the Petitioner, is inadequate in connection with such transportation and services and does not pay a fair and reasonable return on the value or cost of the facilities and property owned and used by the Petitioner for the purpose of said transportation and services or its investment therein.

7. On April 7, 1944, Petitioner received a letter from the Post Office Department, a copy of which is attached hereto and marked Exhibit A, advising Petitioner that because of refusals at Salt Lake City by United Air Lines, the Post Office Department finds it necessary to withhold dispatch of airmail for Chicago, New York and Washington, D. C. Gateways from Petitioner's Route 13. In view of the fact that Petitioner's heaviest mail poundage moves between Los Angeles and Salt Lake City on Route 13, Petitioner estimates that the withholding of the dispatch of such mail from Route 13 will adversely affect Petitioner's mail revenue by an amount of \$125,000.00 per year.

8. In its order of November 8, 1943, which was made retroactively effective January 1, 1943, the rate was fixed

“between the points between which Western Air Lines, Inc. is authorized to carry mail by its certificates of public convenience and necessity.”’. Petitioner is not advised whether this rate was meant to apply to Route 63 for which it was awarded a certificate on August 13, 1943. If the order of November 8, 1943 does not cover the service to be rendered on Route 63, it will be necessary that the Board establish a rate of compensation for the transportation of mail over Route 63.

9. The fair and reasonable rate of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith as performed by the Petitioner on said air mail Routes 13, 19 and 52 is a rate of twenty five cents (25c) per airplane mile and on air mail Route 63 is a rate of 0.3 mill per pound mile of mail carried.

Such rates are needed by the Petitioner as compensation for the transportation of mail and the services in connection therewith performed by it,

(a) in order to insure the performance by the Petitioner of such service as is required under the certificates of public convenience and necessity which Petitioner holds and under which it operates.

(b) to insure the performance by the Petitioner of such service as is required by the standards respecting the character and quality of service to be rendered as prescribed by or pursuant to law, and,

(c) in order to enable the Petitioner under honest, economical and efficient management to maintain and continue the development of air transportation on said routes 13, 19, 52 and 63 to the extent and of the character and quality required by the commerce of the United States, the Postal Service and the National Defense.

The present rates of compensation and the income derived by the Petitioner as a result thereof, and from all other sources, are not adequate for the needs of the Petitioner in said respects or any of them.

4 WHEREFORE, the Petitioner prays that the Board fix a date for a hearing on this application, giving such notice thereof as is provided by law and that upon said hearing the Board enter an order fixing the rates of compensation at not less than the rates specified in Paragraph 9 hereof, and that the rates so fixed for mail schedules on Routes 13, 19 and 52 be made effective as of the date of the filing of this petition and that the Board establish said rate of compensation for Route 63 to become effective as of May 1, 1944.

Respectfully submitted,
 WESTERN AIR LINES, INC.
 By LEO H. DWERLKOTTE
Executive Vice President

Guthrie & Darling
 737 Pacific Mutual Building
 Los Angeles, California
Attorneys for Petitioner

5

EXHIBIT A

POST OFFICE DEPARTMENT
 OFFICE OF ASSISTANT SUPERINTENDANT
 AIR MAIL SERVICE
 SAN FRANCISCO 1, CALIF.

AOW:K

April 7, 1944

SUBJECT: Delay to air mail account refusals at Salt Lake City, Utah

Mr. Ray Grant,
 Western Air Lines, Inc.,
 Los Angeles, 14, California

Dear Sir:

Because of the frequency and the amount of eastbound air mail that has been delayed because of refusals at Salt

Lake City by United Air Lines it becomes necessary to withhold dispatch of air mail for Chicago, New York and Washington, D. C., Gateways from your AM 13 until such time as conditions warrant the return to such routing. This change will become effective April 15th.

We find that during the month of March mail was refused at Salt Lake City as follows:

| | Number Refusals | Trips Cancelled | Passed Over | Total Failures |
|---------|--------------------|--------------------|----------------|-------------------|
| AM 1-26 | 10 | 3 | 0 | 13 |
| AM 1-12 | 11 | 2 | 3 | 18 |
| AM 1-24 | 8 | 5 | 0 | 13 |
| AM 1-2 | 21 | 1 | 1 | 23 |
| AM 1-20 | 20 | 2 | 3 | 25 |
| AM 1-10 | 18 | 4 | 0 | 22 |
| AM 1-28 | 24 | 3 | 1 | 28 |
| AM 1-6 | 23 | 1 | 0 | 24 |

Notwithstanding that refusals and cancellations have occurred also on routes of other carriers, we find by actual check that better service could have been rendered by withholding from AM 13 the mail referred to.

Consideration will be given the return of such mail as soon as conditions warrant.

Very truly yours,
/s/ A. O. WILLOUGHBY
Assistant Superintendent.

cc: Mr. R. M. Martin
Mr. A. C. Hodges
Mr. R. E. Pollard

Filed Feb. 10, 1947

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UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D.C.

Docket No. 1374

In the Matter of the Petition
of

WESTERN AIR LINES, INC., for an order fixing the fair
and reasonable rates of compensation for the trans-
portation of air mail over its routes.

Amendment No. 1

TO THE HONORABLE CIVIL AERONAUTICS BOARD:

Petitioner respectfully amends its petition in the above
captioned proceeding in the following particulars:

I

Paragraph 1 of the petition is amended to read:

1. Petitioner is a corporation duly organized and existing
under the laws of the State of Delaware and is operating as
a common carrier by air and is now the holder of certificates
of convenience and necessity for the transportation of mail,
passengers and property.

II

Paragraph 9 of the petition is amended to read:

9. The fair and reasonable rate of compensation for the
transportation of mail by aircraft, the facilities used and
useful therefor and the services connected therewith as
performed by Petitioner is the sum of twenty-five cents
(25¢) per airplane mile flown by Petitioner over its certi-
fied routes, or the equivalent thereof based on such formula
or method of calculation as may appear to be desirable or
appropriate.

Such rate is needed by Petitioner as compensation for the transportation of mail and the services in connection therewith performed by it since the filing of this petition and to be performed hereafter:

10 (1) in order to insure the performance by Petitioner of such service as is required under the certificates of public convenience and necessity which Petitioner holds and under which it operates;

(2) to insure the performance by Petitioner of such service as is required by the standards respecting the character and quality of service to be rendered as prescribed by or pursuant to law, and,

(3) In order to enable Petitioner under honest, economical, and efficient management to maintain and continue the development of air transportation on its routes to the extent and of the character and quality required by the commerce of the United States, the Postal Service and the National Defense.

III

A new paragraph is added numbered 10 and reading:

10. Events which have occurred since the date of filing of the petition in the within proceeding and prevailing exigencies make it imperative, in order to enable Petitioner to fulfill its duties to the public, that a temporary rate or rates be fixed forthwith as compensation to Petitioner for the transportation of mail by aircraft over its certificated routes effective in the future as well as retroactively to the date of the filing of the petition herein.

IV

A new paragraph is added numbered 11 and reading:

11. Problems confronting Petitioner require that a permanent mail rate in response to this petition be determined and fixed as expeditiously as possible and be made retroactive to May 1, 1944, the date of the filing of this petition, subject to such adjustments as may be necessary

or appropriate to compensate for the temporary rate or rates requested herein to be fixed.

WHEREFORE, Petitioner prays

(1) That pending determination of the permanent rate a temporary air mail rate or rates for Petitioner be fixed forthwith in such manner and amount as may be just
11 and reasonable under the attending circumstances, to be effective in the future as well as retroactively to May 1, 1944, the date of the filing of the petition herein.

(2) That a hearing be called and held as expeditiously as possible for the purpose of fixing and determining the permanent air mail rate for Petitioner in the amount alleged herein to be just and reasonable, or such greater amount as may be found by the Board to be just and reasonable under the circumstances, effective retroactively to the date of the filing of the petition herein, and

(3) That such other, further and enlarged relief be accorded Petitioner as may by the Board be deemed justified in the light of the prevailing circumstances and the evidence submitted.

Respectfully submitted,
WESTERN AIR LINES, INC.
By RONALD C. KINSEY

Guthrie, Darling & Shattuck
737 Pacific Mutual Building
Los Angeles, California

Filed Feb. 24, 1947

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UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 1374

In the Matter of the Petition

of

WESTERN AIR LINES, INC., for an order fixing the fair and reasonable rates of compensation for the transportation of air mail over its routes.

Amendment No. 2

TO THE HONORABLE CIVIL AERONAUTICS BOARD:

Petitioner respectfully amends its petition in the above captioned proceeding and represents as follows:

I

Petitioner filed its original application in this proceeding on or about April 26, 1944, and filed Amendment No. 1 thereto on or about February 9, 1947.

II

Petitioner's present cash position and the operating losses which Petitioner has been experiencing and which Petitioner estimates it will continue to experience, make it imperative for Petitioner to obtain immediate relief through the establishment of a temporary emergency airmail rate to be reviewed at a later date after a full hearing is held and a permanent mail rate is fixed for Petitioner's system.

III

Petitioner's present cash position is critical, and immediate relief must be obtained if Petitioner is to continue to provide the service required under Section 406 of the Civil Aeronautics Act of 1938.

IV

Petitioner's operating losses have been occasioned by a rapidly declining Passenger Load Factor since August 1946, and have been augmented by a severe decline in Operating Performance since October 1946. See Exhibit "A" attached hereto.

V

Petitioner curtailed schedules as the demand for seats fell off, but Load Factors continued to decline even after schedules were reduced. See Exhibit "B" attached hereto.

VI

Petitioner has experienced substantial Operating Losses during the last four months. See Exhibit "C" attached hereto.

VII

Petitioner has been unsuccessful in its attempts to obtain additional Equity Financing or Cash Loans. See Exhibit "D" attached hereto.

VIII

Petitioner has embarked on an extensive Cost Reduction Program which includes a material reduction in personnel, a curtailment of its advertising program, consolidation of general offices, elimination of certain traffic offices, and consolidation of ground services with other carriers, and such further Cost Reductions as can be effected without impairing the safety of operations are under consideration. See Exhibit "E" attached hereto.

IX

Petitioner will be unable to carry on operations for the length of time required for a routine hearing on its original application as amended.

16A WHEREFORE, Petitioner prays

(1) That an immediate emergency hearing be held and a temporary emergency air mail rate be fixed and determined.

(2) That such hearing be held and such emergency rate be fixed and determined for the future and retroactive for such period as the Board may deem appropriate without prejudice to the later determination of a permanent air mail rate prayed for in the original petition as amended.

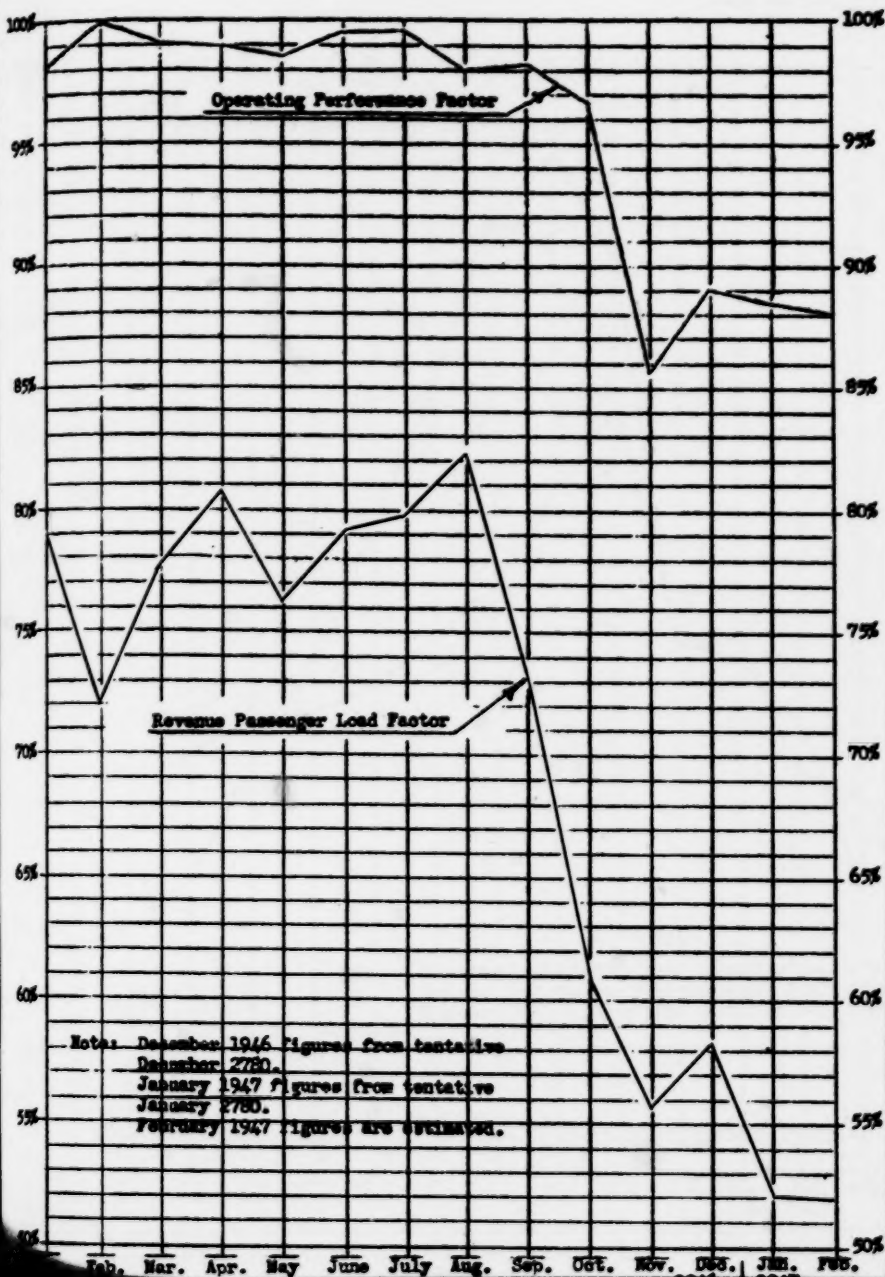
(3) That such other further and enlarged relief be accorded Petitioner as may by the Board be deemed justified in the light of the prevailing circumstances and the evidence submitted.

Respectfully submitted,
WESTERN AIR LINES, INC.
By Paul E. Sullivan

Guthrie, Darling & Shattuck
737 Pacific Mutual Building
Los Angeles, California

WESTERN AIR LINES, INC.

Exhibit No. W-4
Page No. 1



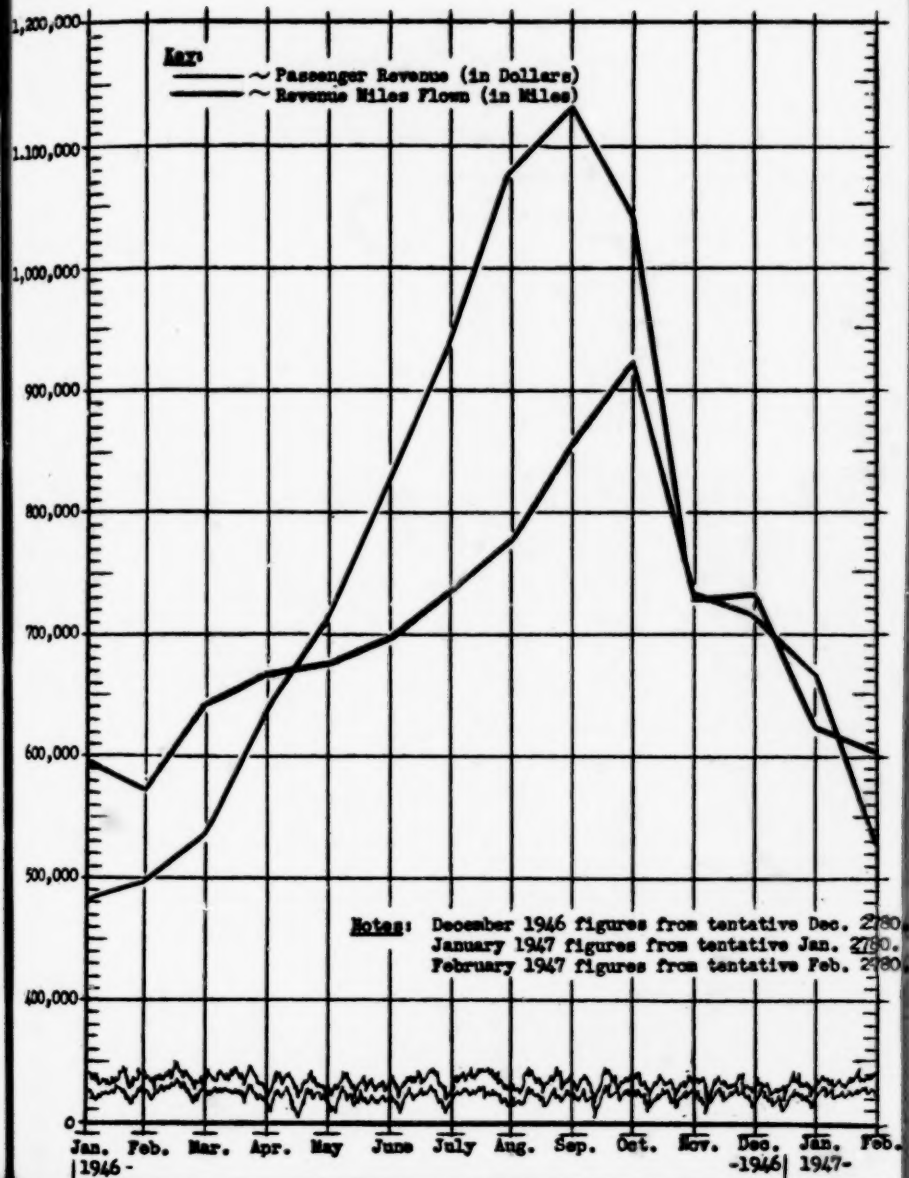
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1912-1913

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WESTERN AIR LINES, INC.

Exhibit No. B
Page No. 1



Source: Civil Aeronautics Board, Form 2780, Schedule 3, Western Air Lines.

Exhibit C

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WESTERN AIR LINES, INC.

STATEMENT OF PROFIT AND LOSS
For the Periods Indicated

(To the nearest thousand dollars)

| | November 1946 (Actual) | December* 1946 (Tenta- tive) | January 1947 (Esti- mated) | February 1947 (Esti- mated) |
|--|------------------------------|---------------------------------------|-------------------------------------|--------------------------------------|
| Revenues: | | | | |
| Passenger | \$ 727,000 | 733,000 | 718,000 | 651,000 |
| Mail | 38,000 | 49,000 | 30,000 | 24,000 |
| Other | 39,000 | 55,000 | 19,000 | 17,000 |
| Total transportation revenue | 804,000 | 837,000 | 767,000 | 692,000 |
| Total incidental revenue | 7,000 | 13,000 | 5,000 | 5,000 |
| Total operating revenues | 811,000 | 850,000 | 772,000 | 697,000 |
| Operating expenses: | | | | |
| Flight operations | 222,000 | 227,000 | 179,000 | 155,000 |
| Direct Maintenance—Flight Equipment | 177,000 | 273,000 | 150,000 | 130,000 |
| Depreciation—Flight Equipment | 141,000 | 149,000 | 141,000 | 140,000 |
| Total | 540,000 | 649,000 | 470,000 | 425,000 |
| Ground operations | 189,000 | 246,000 | 175,000 | 162,000 |
| Ground & indirect maintenance | 97,000 | 72,000 | 82,000 | 82,000 |
| Passenger service | 75,000 | 87,000 | 68,000 | 65,000 |
| Traffic and sales | 106,000 | 110,000 | 112,000 | 112,000 |
| Advertising and publicity | 48,000 | 33,000 | 22,000 | 22,000 |
| General and administrative | 83,000 | 103,000 | 80,000 | 80,000 |
| Depreciation—other property | 12,000 | 12,000 | 12,000 | 12,000 |
| Total | 610,000 | 663,000 | 551,000 | 535,000 |
| Total operating expenses | 1,150,000 | 1,312,000 | 1,021,000 | 960,000 |
| Net operating income | (339,000) | (462,000) | (249,000) | (263,000) |
| Net operating income or (expense) | 106,000 | (29,000) | (10,000) | (10,000) |
| Net income before taxes | (233,000) | (491,000) | (259,000) | (273,000) |
| Federal income tax provision or (credit) | (93,000) | (82,000) | — | — |
| Net profit or (loss) | (140,000) | (409,000)* | (259,000) | (273,000) |

* No provision has been made herein for expenses of attempted financing which are presently estimated to be approximately \$100,000.00. A subsequent adjustment as of December 31, 1946 is anticipated.

Exhibit "D"**WESTERN AIR LINES, INC.****EQUITY FINANCING AND CASH BORROWINGS ATTEMPTED**

Prior to the end of the war, Petitioner began to formulate an equipment and facilities program for the postwar years. This program as ultimately developed contemplated the expenditure of approximately \$20,000,000.00 for new equipment and facilities.

Early in 1946, negotiations were undertaken with a group of Eastern banks which evidenced their willingness to make available to Petitioner, until March 31, 1948, a credit of \$20,000,000.00 for the purpose of purchasing Flying Equipment.

The loans were to be made as funds were required by Petitioner against notes secured by chattel mortgages on Flying Equipment. The notes were to be payable over periods of five years from date, 20% one year after date and the balance in eight equal semi-annual installments.

Terms of the proposed financing agreement were drafted and submitted for consideration of the parties. In addition to submission to Petitioner and the Agent Bank, the Loan Agreement was studied by Counsel for Petitioner as well as by Counsel for the Agent Bank and by Counsel for proposed participating banks. This all required considerable time and during the course of the negotiations the banks loaned Petitioner a total of \$3,000,000.00

When Petitioner required additional funds in August 1946, there was an apparent hesitancy on the part of the banks to make such funds available until the loan agreement had been signed. Representatives of the banks came to Los Angeles late in September supposedly to execute the Loan Agreement. At that time, they notified Petitioner that they were unwilling to make any additional loans until after Petitioner had obtained additional equity capital from the sale of stock. Petitioner had sold Capital Stock in
23 January 1946 for which it had received approximately \$2,200,000.00.

In order to sell the amount of additional stock required, it was necessary for Petitioner to have a Special Meeting of Shareholders to amend its Certificate of Incorporation and to file a Registration Statement with the Securities and Exchange Commission.

Realizing that both of these procedures would take considerable time, Petitioner continued its efforts to obtain additional private capital either through investment or by borrowing.

At that time, however, the stock market was continuing to decline and airline stocks were particularly unattractive because of the poor earnings record established in the first half of the year. The airlines were beset by a series of unfortunate occurrences, including the grounding of the Lockheed Constellations, Pilots' strikes, unfavorable and wide spread publicity concerning crashes, both domestic and foreign, scheduled and non-scheduled, as well as generally adverse publicity concerning airline service. Petitioner's efforts to secure either equity or loan financing were without avail.

During November a tentative arrangement was worked out with a New York Investment House contemplating the sale of stock to net Petitioner at least \$6,500,000.00 whereupon the Banks were to loan Petitioner up to \$7,500,000.00.

A Registration Statement was filed with the Securities and Exchange Commission on November 27, 1946, with the hope of making a public offering on or about December 18. When that date arrived the proposed Underwriting Group decided to postpone the public offering until after the first of the year.

24 After standing by during the month of January, Petitioner was advised by the Underwriters on January 31, 1947, that they found it impossible to proceed with a public offering of airline stock at this time.

Petitioner has continued its efforts to obtain private funds without success.

During the course of all these negotiations, Petitioner cut its new equipment program in half and arranged deferment

of deliveries on the remaining half. It also converted most of its major obligations to a secured basis and has arranged short term extensions, from time to time, of the due dates of these secured obligations. A cash borrowing of \$600,000.00 was obtained from a private source on a secured basis. The principal stockholder of Petitioner pledged 70,000 shares of the stock of Petitioner owned by him as security for an obligation of Petitioner and accepted a second chattel mortgage on aircraft as security therefor.

Petitioner has submitted an application for a loan from the Reconstruction Finance Corporation, which application is presently being processed by that agency.

25

Exhibit E**COST REDUCTION PROGRAM**

Western Air Lines, Inc. has made and is making every effort to reduce expenses and costs wherever possible. Effective January 1, 1946, the Company established a new department known as the budget and cost control department. This department had developed an improved budget and cost control system which has played a substantial part in the recent economies which have been effected by the Company. This department is engaged in extensive industrial engineering work and has effected considerable savings through improved procedures and methods. Every effort is being made by the company to eliminate all items of expense or costs which are not absolutely essential to present operations.

As of October 31, 1946, Western Air Lines, Inc. had 2,373 employees on its payroll. As of February 18, 1947 the number of employees on the payroll had been reduced to 1,950. This represents a reduction of approximately 18 per cent in the number of employees. Since February 18, further reductions in personnel have been effected. The number of employees in the advertising department have been reduced to three, and likewise the number of employees in the publicity department have been reduced to three.

The management of the Company has recently issued a freeze order on the hiring of additional personnel, and even replacements must have the approval of the president or the executive vice president.

The Company is in the process of moving its main base of operations from the Lockheed Air Terminal to a new hangar and operations office at the Los Angeles Airport. Due to the fact that this building will not be completed for several months, the Company is faced with the unavoidable cost of split operations. It is anticipated that when the main base of operations is completely moved to the Los Angeles Airport and the improved facilities at that point have been made available to the Company's personnel, substantial savings in maintenance and ground operations costs will be effected.

As one indication of the problem with which the Company is presently confronted at Lockheed Air Terminal, the Company has found it necessary to maintain eight different
26 stock rooms because of the widely scattered maintenance operations. All of these operations will be combined in the new hangar, and it is estimated that at least 50 to 60 per cent of present stock room personnel will be eliminated.

For a period of many years, the Company has had its engine overhaul work performed by an outside concern. Concurrently with the move to Los Angeles Airport, the Company had planned to establish its own engine overhaul shops, anticipating thereby to effect substantial economies in engine overhaul costs. In view of the Company's critical financial situation and the Company's inability to secure adequate financing, the establishment of the engine overhaul shop has been postponed and all orders for equipment and facilities for the engine overhaul shop have been cancelled wherever possible. Although the Company is still of the opinion that the establishment of an engine overhaul shop is essential to the reduction of engine overhaul costs, it is impossible to undertake the program until adequate funds are available.

In November of 1946, the Company consolidated its general offices in a war surplus building in Beverly Hills, thereby enabling it to eliminate the high cost rental of office space previously occupied in Los Angeles, Hollywood and Burbank. The annual savings effected through reduced rentals, increased efficiency, elimination of dual facilities and personnel such as dual switchboard operators and messengers, telephone lines, etc. is estimated at approximately \$100,000.00 per annum. The Company has substantially reduced its advertising program and has eliminated certain phases of advertising such as the photographic department, the display and exhibits department, and the Company house organ.

Further economies which have been or are in the process of being effected include the closing of certain city traffic offices and the consolidation of ground services with other air carriers.

The Company is presently pursuing a policy of reducing costs and expenses in every way possible without impairing the safety of operations.

(Filed Mar. 11, 1947)

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UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 1374

In the Matter of the Petition

of

WESTERN AIR LINES, INC., for an order fixing the fair and reasonable rates of compensation for the transportation of air mail over its routes Nos. 13, 19, 52, 63 and 68.

Amendment No. 3

TO THE HONORABLE CIVIL AERONAUTICS BOARD:

Petitioner respectfully further amends its Petition in the above captioned proceeding in the following particulars:

I

Paragraph I of Amendment No. 2 is amended to read:

Petitioner filed its original application in this proceeding on or about April 26, 1944, Amendment No. 1 thereto on or about February 8, 1947 and Amendment No. 2 thereto on or about February 24, 1947.

II

Paragraph III of Amendment No. 2 is amended to read:

Petitioner's present cash position is critical and immediate relief must be obtained if Petitioner is to continue to provide the service required under Section 406 of the Civil Aeronautics Act of 1938, as amended. See copy of Affidavit of Treasurer, Balance Sheet at December 31, 1946, Profit and Loss Statement for the year 1946 and Annual Report to Stockholders for 1945 attached hereto.

29 WHEREFORE, Petitioner prays

(1) That an immediate emergency hearing be held and a temporary emergency air mail rate be fixed and determined.

(2) That such hearing be held and such emergency rate be fixed and determined for the future and retroactive for such period as the Board may deem appropriate without prejudice to the later determination of the permanent air mail rate prayed for in the original petition as amended.

(3) That such other further and enlarged relief be accorded Petitioner as may by the Board be deemed justified in the light of the prevailing circumstances and the evidence submitted.

Respectfully submitted,
WESTERN AIR LINES, INC.
By Paul E. Sullivan

Guthrie, Darling & Shattuck
737 Pacific Mutual Building
Los Angeles, California

* * * * * * * * *

32 STATE OF CALIFORNIA,
 COUNTY OF LOS ANGELES, ss:

Affidavit of J. J. Taylor

J. J. Taylor, Treasurer of Western Air Lines, inc., being first duly sworn on oath, deposes and says:

1. That from an inspection of the books and records of the Company as at the close of business, December 31, 1946, the current assets amounted to \$3,919,414.34; the current liabilities amounted to \$8,618,776.96 and the working capital deficit as of that date was therefore \$4,699,362.62.

2. That the cash in banks and on hand as of the close of business December 31, 1946 amounted to \$1,047,210.44, of which \$402,000.00 was held in trust by a bank as collateral for a loan.

3. That cash in banks as of the close of business February 19, 1947 amounted to \$320,123.82 exclusive of \$402,000.00 held by a bank as collateral.

4. That for the year 1946, Western Air Lines, Inc. has suffered a net operating loss before tax adjustments of \$1,073,557.67 and a net loss after tax adjustments of \$811,823.92, as reported on CAB Forms 2780. That said loss for the year 1946 may be further increased by expenses of attempted financing during the last quarter of 1946, the amount of such expenses being presently unknown but presently estimated at approximately \$100,000.00.

5. That Western Air Lines, Inc. has suffered a net loss, after tax adjustments, as reported on CAB Forms 2780, of \$139,926.56 for November, 1946, of \$409,025.35 for December, 1946, and that the anticipated net loss for January, 1947 is estimated at approximately \$259,000.00 and the anticipated net loss for February, 1947 is forecast to be approximately \$273,000.00.

6. That Western Air Lines, Inc. net cash loss for November, 1946 was \$80,983.40, for December, 1946, \$330,374.81, and the anticipated net cash loss from operations for January, 1947 is estimated at \$97,000.00 and for February, 1947 is estimated at \$111,000.00.

33 7. That from an inspection of the books, records, and contracts of the Company, he has forecast the cash requirements of Western Air Lines, Inc. for the period from and after December 31, 1946 to and including April 30, 1947; and that said forecast is as follows:

WESTERN AIR LINES, INC.

FORECAST OF CASH REQUIREMENTS

| Estimated | January 1947 | February 1947 | March 1947 | April 1947 |
|--|-----------------|------------------|---------------|---------------|
| Operating expenses (less depreciation) | \$868,000 | \$ 808,000 | \$ 852,000 | \$ 863,000 |
| Less estimated revenue (passenger, mail, express, freight and incidental) | 771,000 | 697,000 | 825,000 | 891,000 |
| Cash loss from operations | 97,000 | 111,000 | 27,000 | (28,000) |
| Other cash requirements: | | | | |
| Notes payable due Feb. 10, 1947: | | | | |
| Tradesmens National Bank | | 3,000,000(a) | | |
| Douglas Aircraft Company | | 1,659,414(a) | | |
| Federal Engineering Corp. | | 600,000(a) | | |
| Purchase contract—8 C-54 aircraft from War Assets Corp. | 11,232 | 11,232 | 11,232 | 11,232 |
| Austin Co., balance on construction of L.A. Airport hangar | | 813,000(a) | 100,000 | 100,000 |
| Past due accounts payable: | | | | |
| October 1946 vouchers | | 26,000 | | |
| November 1946 vouchers | | 226,000 | | |
| December 1946 vouchers | | 606,000 | | |
| Pacific Airmotive, engine overhaul costs unaudited to date | | 183,000 | | |
| Progress payment on 10 Convair "240" aircraft | | | 86,675(a) | |
| Total cash deficit | \$108,232 | 7,235,646 | 224,907 | 83,232 |
| Cumulative cash deficit | \$108,232 | 7,343,878 | 7,568,785 | 7,652,017 |

Notes:

(a) Negotiations are presently in progress with these and other creditors to obtain extensions of the due dates of these obligations. The Company also has made and is making every effort to cancel, defer or reduce all orders and commitments for new equipment and other items which are not essential to the immediate present operation. As later explained in more detail, the Company has made extensive attempts to obtain equity financing without success. Attention is directed to the fact that some additional cash outlay may be necessary in addition to the above schedule because of cancellation charges on orders, our inability to cancel such orders, etc.

Obviously, an increased mail rate alone will not solve Western's problem. A loan has been requested from the Reconstruction Finance Corporation until such time as permanent equity financing can be completed.

34 and that a statement of current assets and current liabilities as of November 30, 1946 as reflected on the books and records of Western Air Lines, Inc. is as follows:

WESTERN AIR LINES, INC.

CURRENT ASSETS AND CURRENT LIABILITIES
AS AT DECEMBER 31, 1946

Current Assets

| | | |
|-----|-------------------------------------|-----------------|
| 101 | Cash | \$1,047,210.44* |
| 102 | Working funds and special deposits | |
| | (a) Working fund advances | 15,223.17 |
| 103 | Short term securities | |
| | (a) U. S. Government securities | — |
| 104 | Accounts receivable: | |
| | (a) U. S. mail pay | 126,245.99 |
| | (b) U. S. Government departments | 401,595.51 |
| | (c) Air travel plan | 84,463.33 |
| | (d) Other accounts receivable | 291,621.05 |
| | | <hr/> |
| | | 903,925.78 |
| 105 | Airline traffic accounts receivable | 979,758.54 |
| 106 | Net balances receivable from agents | 11,502.31 |
| 107 | Interest and dividends receivable | — |
| 110 | Materials and supplies | 923,666.70 |
| 111 | Motor fuels | 19,836.39 |
| 112 | Lubricating oils | 1,903.31 |
| 113 | Other current and accrued assets | 16,387.70 |
| | | <hr/> |
| | Total current assets | \$3,919,414.34 |

Current Liabilities

| | | |
|-----|---|----------------|
| 201 | Notes payable | \$3,830,785.36 |
| 202 | Accounts payable | 3,281,123.42 |
| 203 | Airline traffic accounts payable | 582,114.24 |
| 204 | Air travel plan liability | 238,850.00 |
| 206 | Salaries and wages accrued | 348,028.92 |
| 207 | Interest accrued | 1,624.47 |
| 208 | Taxes accrued | 260,331.96 |
| 209 | Ticket refund liability | 35,960.28 |
| 210 | Other current and accrued liabilities | 39,958.31 |
| | | <hr/> |
| | Total current liabilities | \$8,618,776.96 |
| | Excess of current liabilities over current assets | \$4,699,362.62 |

* Includes \$402,000.00 cash held as collateral by a bank.

Note—Subject to public auditor's adjustments.

35 8. That from the statement of current assets and current liabilities as of the close of business December 31, 1946, and from the forecast of cash requirements for the period from and after December 31, 1946, it is apparent that Western Air Lines, Inc. is momentarily in danger of being unable to carry on its operations because of insufficient cash and working capital.

9. That Western Air Lines, Inc. has made every effort within its means to secure additional sources of cash; that

all of said sources have been exhausted by previous financing, and that unless said Western Air Lines, Inc. is granted an increase in its rate of compensation for the transportation of mail, will be unable to obtain the financing which will be necessary in order to enable Western Air Lines, Inc. to continue operations.

10. That the foregoing has been prepared under his supervision and direction from the books and records of the Company and to the best of his belief and knowledge the statements contained herein and set forth in said statements of assets and current liabilities and said forecast of cash requirements fairly present the status of Western Air Lines, Inc. as to the dates referred to in accordance with the Uniform System of Accounts for Domestic Air Carriers prescribed by the Civil Aeronautics Board.

J. J. TAYLOR, *Treasurer*
WESTERN AIR LINES, INC.

Subscribed and sworn to before me, a Notary Public in and for said County and State, this 21st day of February, 1947

C. W. Kolling,
Notary Public

[Seal]

My Commission Expires March 18, 1950.

Schedule 1—Page 1 of 2

36 CAB Form 2780

WESTERN AIR LINES, INC.

(Name of Air Carrier)

BALANCE SHEET (TENTATIVE) As at December 31, 1946

| Acct. No. | Assets | Amount | Total |
|--|---|----------------|----------------------|
| Current Assets: | | | |
| 101 | Cash | \$1,047,210.44 | \$ |
| 102 | Working funds and special deposits: | | |
| | (a) Working fund advances | \$ 15,223.17 | |
| | (b) Special deposits | 15,223.17 | |
| 103 | Short-term securities: | | |
| | (a) U. S. Government securities | | |
| | (b) Other short-term securities | — | |
| 104 | Accounts receivable: | | |
| | (a) U. S. Mail pay | 126,245.99 | |
| | (b) U. S. Government depts. | 401,595.41 | |
| | (c) Air travel plan | 84,463.33 | |
| | (d) Other accounts receivable | 291,621.05 | |
| 105 | Airline traffic accounts receivable | 903,925.78 | |
| 106 | Net balances receivable from agents | 979,758.54 | |
| 107 | Interest and dividends receivable | 11,502.31 | |
| 108 | Notes receivable | — | |
| 109 | Subscriptions to capital stock | — | |
| 110 | Materials and supplies | 923,666.70 | |
| 111 | Motor fuels | 19,836.39 | |
| 112 | Lubricating oils | 1,903.31 | |
| 113 | Other current and accrued assets | 16,387.70 | 3,919,414.34 |
| Investments and Special Funds: | | | |
| 121 | Investments | 2,024.34 | |
| 122 | Investments in and advances to affiliates | 437,672.05 | |
| 123 | Net investment in separately operated divisions | — | |
| 124 | Uninsured losses—funds | — | |
| 125 | Other special funds | 653,658.18 | 1,093,354.57 |
| Operating Property and Equipment: | | | |
| 150 | Flight equipment | \$5,734,594.84 | |
| 250 | Less: Accrued Depreciation | 1,857,629.62 | 3,876,965.22 |
| 150 | Other property and equipment | 1,269,332.57 | |
| 250 | Less: Accrued Depreciation | 396,557.68 | 872,774.89 |
| 150 | Land | 60,923.95 | |
| 150 | Construction work in progress | 2,638,321.31 | 7,448,985.37 |
| 160 | Nonoperating Property and Equipment | 41,501.86 | |
| 260 | Less: Accrued depreciation | 808.25 | 40,693.61 |
| Deferred Charges: | | | |
| 171 | Prepayments | 315,980.93 | |
| 172 | Extension and development projects | — | |
| 173 | Unamortized discount and expense on debt | — | |
| 174 | Long-term operating property prepayments | 455.28 | |
| 175 | Other deferred charges | 239,800.15 | 556,236.36 |
| Intangibles: | | | |
| 181 | Property acquisition adjustment | — | |
| 182 | Other intangibles | 1.00 | 1.00 |
| Capital Stock Discount and Expense: | | | |
| 191 | Capital stock discount | | |
| 192 | Capital stock expense | | — |
| Total Assets | | | 13,058,685.25 |

Schedule 1—Page 2 of 2

37

WESTERN AIR LINES, INC.

(Name of Air Carrier)

BALANCE SHEET (TENTATIVE) As at December 31, 1946

| Acct. No. | Liabilities and Capital | Amount | Total |
|--------------|---------------------------------------|----------------|---------------|
| | Current Liabilities | | |
| 201 | Notes payable | \$3,830,785.36 | \$ |
| 202 | Accounts payable | 3,281,123.42 | |
| 203 | Airline traffic accounts payable | 582,114.24 | |
| 204 | Air travel plan liability | 238,850.00 | |
| 205 | Dividends declared | — | |
| 206 | Salaries and wages accrued | 348,028.92 | |
| 207 | Interest accrued | 1,624.47 | |
| 208 | Taxes accrued | 260,331.96 | |
| 209 | Ticket refund liability | 35,960.28 | |
| 210 | Other current and accrued liabilities | 39,958.31 | 8,618,776.96 |
| | Long-Term Debt: | | |
| 221 | Long-term debt | 287,106.60 | 287,106.60 |
| 222 | Advances from affiliates | — | |
| | Deferred Credits: | | |
| 231 | Unearned transportation revenue | 228,619.39 | |
| 232 | Installments on capital stock | 18,212.03 | |
| 233 | Unamortized premium on debt | — | |
| 234 | Other deferred credits | 25,352.93 | 272,184.35 |
| | Operating Reserves: | | |
| 271 | Reserve for aircraft overhaul | 76,494.50 | |
| 272 | Reserve for aircraft engine overhaul | 229,543.20 | |
| 273 | Reserve for pensions | — | |
| 274 | Other operating reserves | 62,100.00 | 368,137.70 |
| | Capital Stock: | | |
| 281 | Preferred stock—par value, \$..... | | |
| | Outstanding..... shares..... | | |
| 282 | Common stock—par value, \$1.00 | | |
| | Outstanding 525,164 shares..... | 525,164.00 | |
| 283 | Preferred stock—no par value | | |
| | Outstanding..... shares..... | | |
| 284 | Common stock—no par value | | |
| | Outstanding..... shares..... | | |
| 286 | Capital stock subscribed and unissued | | 525,164.00 |
| | Surplus: | | |
| 291 | Reserve for uninsured losses | | |
| 292 | Other surplus reserves | | |
| 293 | Capital surplus | 2,768,247.10 | |
| 294 | Unappropriated earned surplus | 1,030,892.46 | |
| | Profit or loss—year to date | (811,823.92) | 2,987,315.64 |
| | Total Liabilities and Capital | | 13,058,685.25 |

Schedule 3 Page 1 of 1

38

WESTERN AIR LINES, INC.

(Name of Air Carrier)

STATEMENT OF PROFIT AND LOSS

TENTATIVE

Month of December 31, 1946

| Acct. No. | Account (1) | Current Month | | Year to Date | |
|--------------|-------------------------------------|---------------|----------------------------------|----------------|----------------------------------|
| | | Amount (2) | Cents Per Rev. Mile (3) | Amount (4) | Cents Per Rev. Mile (5) |
| | REVENUE MILES FLOWN | 716,694 | | 8,613,585 | |
| | OPERATING REVENUES | | | | |
| | Transportation: | | | | |
| 301 | Passenger | \$732,950.41 | 102.27 | \$9,358,149.38 | 108.64 |
| 302 | Mail: | | | | |
| | (a) United States Gov't. | 49,293.42 | 06.88 | 388,146.95 | 04.51 |
| | (b) Foreign governments | — | — | — | — |
| 303 | Express and freight: | | | | |
| | (a) Express | 27,994.39 | 03.90 | 173,324.47 | 02.01 |
| | (b) Freight | 10,760.96 | 01.50 | 56,623.57 | 00.66 |
| 304 | Excess baggage | 5,923.48 | 00.83 | 67,756.02 | 00.79 |
| 305 | Charter and special | 9,522.20 | 01.33 | 19,598.66 | 00.23 |
| 306 | Other transportation | 112.56 | 00.01 | 307.51 | — |
| 300 | Total Transportation | 836,557.42 | 116.72 | 10,063,906.56 | 116.84 |
| | Incidental Revenues—Net: | | | | |
| 351 | Restaurant and food services—net | 4,350.82 | 00.61 | 41,702.21 | 00.48 |
| 352 | Service sales—net | 5,194.79 | 00.72 | 41,537.94 | 00.48 |
| 353 | Rental from operating property—net | 2,558.11 | 00.36 | 23,808.38 | 00.28 |
| 354 | Limousine service—net | — | — | — | — |
| 355 | Other incidental revenues—net | 1,425.60 | 00.20 | 5,492.54 | 00.06 |
| 350 | Total Incidental Revenues—Net | 13,529.32 | 01.89 | 112,541.07 | 01.30 |
| | Total Operating Revenues | 850,086.74 | 118.61 | 10,176,447.63 | 118.14 |
| | OPERATING EXPENSES | | | | |
| 400 | Flying operations | 227,012.53 | 31.67 | 2,092,779.44 | 24.30 |
| 500 | Flight equipment maintenance—direct | 272,594.65 | 38.04 | 1,731,819.07 | 20.10 |
| 850 | Depreciation—Flight equipment | 149,152.52 | 20.81 | 1,126,514.45 | 13.08 |
| | Total | 648,759.70 | 90.52 | 4,951,112.96 | 57.48 |
| 450 | Ground operations | 246,544.70 | 34.40 | 2,025,280.59 | 23.51 |
| 550 | Ground equipment maintenance—direct | 19,669.95 | 02.74 | 141,116.23 | 01.64 |
| 600 | Equipment maintenance—indirect | 52,278.72 | 07.30 | 703,385.70 | 08.17 |
| 650 | Passenger service | 86,980.40 | 12.14 | 900,958.25 | 10.46 |
| 700 | Traffic and sales | 110,111.13 | 15.36 | 1,083,217.09 | 12.57 |
| 750 | Advertising and publicity | 32,880.84 | 04.59 | 448,329.16 | 05.20 |
| 800 | General and administrative | 103,028.64 | 14.38 | 896,965.02 | 10.41 |
| 850 | Depreciation—ground equipment | 12,068.45 | 01.68 | 99,640.30 | 01.16 |
| | Total Operating Expenses | 1,312,322.53 | 183.11 | 11,250,005.30 | 130.60 |
| | Net operating income | 462,235.79 | 64.50 | 1,073,557.67 | 12.46 |
| 900 | Nonoperating income | 305.75 | x x x | 150,944.36 | x x x |
| | Gross income | 461,930.04 | x x x | 922,613.31 | x x x |
| 950 | Deductions from gross income | 29,665.74 | x x x | 148,249.21 | x x x |
| | Net income before income taxes | 491,595.78 | x x x | 1,070,862.52 | x x x |
| 960 | Income taxes | 82,570.43 | x x x | 259,038.60 | x x x |
| | Net Profit or Loss for Period | 409,025.35 | x x x | 811,823.92 | x x x |

Note: No provision has been made herein for expenses of attempted financing which are presently estimated to be approximately \$100,000.00. A subsequent adjustment as of December 31, 1946 is anticipated.

• • • • •

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Order
Serial Number E-484UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 1374

At a session of the Civil Aeronautics Board
held at its office in Washington, D. C.
on the 29th day of April, 1947.

In the matter of compensation for the transportation of
mail by aircraft, the facilities used and useful therefor,
and the services connected therewith of
WESTERN AIR LINES, INC.
over Routes No. 13, 19, 52, 63 and 68

**Order Fixing and Determining the Fair and Reasonable
Temporary Rate of Compensation For the Transportation
of Mail by Aircraft**

Western Air Lines, Inc (hereinafter called Western) having on April 26, 1944 filed a petition which as amended on February 10, 1947, February 24, 1947 and March 11, 1947, requested the establishment over its entire domestic system of a permanent mail rate of 25 cents per airplane mile flown and a temporary emergency mail rate retroactive for such period and in such amount as the Board may deem appropriate, to serve as a provisional and immediate basis of payment pending the determination of a fair and reasonable final rate in this proceeding;

393 Public hearing having been held in the above-entitled proceeding on March 17 and 18, 1947, and the Board, upon consideration of the record, finding that:

1. Upon the bases of comparison set forth in Appendix No. 1, attached hereto and made a part hereof, the inherent characteristics of Western's routes seem to indicate that Western is basically comparable with other domestic car-

riers in the class now being paid a mail rate of 60 cents per ton-mile;

2. As is shown by Appendix No. 2, attached hereto and made a part hereof, the costs reported by Western are somewhat higher than the average reported costs of other carriers in this class for the calendar year, 1946;

3. Western, as is reflected in Appendix No. 2, appears to have expanded substantially its equipment capacity by acquiring large capacity four-engine aircraft to meet an early post-war demand and has recently suffered a heavy decline in traffic;

4. Western's relatively great number of four-engine large capacity aircraft would appear to have introduced difficulties in scheduling its operations so as to maintain reasonable load factors for such aircraft;

5. Certain conditions now prevailing in the air transportation industry are of such complexity and recent origin as not to permit an immediate and exact evaluation of the extent to which costs related to the volume of Western's
394 statutory standard of honest, economical and efficient operations may reasonably be justified under the management as applied during a period of such abnormal character;

6. The volume of mail carried by Western has declined to such an extent that the petitioner's total mail compensation at its existing rate has been seriously reduced in relation to the reasonable overall volume of services operated;

7. Western apparently has a need for additional mail compensation as measured by the standards established by section 406(b) of the Act;

8. Western's need for mail compensation for its operation conducted in reasonable volume is substantially less than the temporary mail rates requested by the petitioner;

9. Western's financial position is apparently critical and the failure to increase immediately the rate of mail com-

compensation may hamper the ability of the carrier to perform the services which appear to be required in the public convenience and necessity;

10. A final rate could not properly be established in time to provide Western with the immediate relief required;

11. The establishment of a temporary rate of mail compensation for Western to serve as a basis of payment until such time as a fair and reasonable final rate is fixed and determined, is in the public interest;

12. Western's need for mail compensation can be met over a limited period without any necessity for altering indefinitely its status as a service rate carrier, and the mail compensation provided herein does not permanently
395 supplant the basic mail rate of 60 cents per ton mile now in effect;

IT IS ORDERED, That the fair and reasonable temporary rates to be used as a basis of payment on and after October 1, 1946 for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, between the points between which Western Air Lines, Inc., presently is or may hereafter be authorized to transport mail over Routes No. 13, 19, 52, 63 and 68 is hereby fixed, determined and published to be as follows:

(a) For the period October 1, 1946 through February 28, 1947, a total amount of \$687,000.¹

(b) On and after March 1, 1947, a rate of 60 cents per ton-mile, or fraction thereof, of mail carried, computed monthly on the direct airport-to-airport mileage; provided, however, that for the purposes of computing compensation pursuant to this order in no event shall the ton-miles be less than the ton-miles computed as follows:

¹ The sum of compensation was derived by the application of the mail rate of 60 cents per ton-mile to a minimum capacity factor as defined in (b) (1) of 700 pounds per airplane mile flown during the three-month period ended December 31, 1946 and of 600 pounds per airplane mile flown during the two-month period ended February 28, 1947, on schedules designated by the Postmaster General for the carriage of mail.

(1) For any month during which the average daily designated mileage does not exceed 21,000 miles, the ton-miles of mail computed as though the average load per airplane mile flown was not less than the number of pounds set forth below for the respective periods indicated, which number of pounds will be known as the minimum capacity factor:

| | Minimum Capacity Factor |
|--------------------------------------|------------------------------------|
| March 1, 1947 through March 31, 1947 | 600 pounds |
| April 1, 1947 through June 30, 1947 | 500 pounds |
| July 1, 1947 through March 31, 1948 | 400 pounds |
| April 1, 1948 through June 30, 1948 | 300 pounds |
| On and after July 1, 1948 | 250 pounds |

(2) For each month during which the average daily designated mileage exceeds 21,000 miles, the ton-miles of mail computed as though the average load per airplane mile flown was a minimum capacity factor which bears the same relation to the minimum capacity factor specified in (1) above for the respective period as 21,000 miles bears to the average daily designated mileage, except that in no case shall the minimum capacity factor be less than 250 pounds.

The mail compensation derived by the application of the aforesaid rates shall be inclusive of, and not in addition to, the mail compensation heretofore received by Western for mail transported on and after October 1, 1946.

397 The aforesaid minimum capacity factors per airplane mile shall be applied to the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster General for the carriage of mail; provided, however, that if any scheduled flight is operated in two or more sections between any two points served for mail and mail is transported on more than one such section, the aggregate of the sections so used shall, for all purposes of deriving compensation pursuant to this order, be treated as a single flight, and the aggregate mail load actually carried on all such sections or the minimum

capacity factor for one such section, whichever is greater, shall be applied to the airport-to-airport mileage flown by that section which covers the greatest airport-to-airport mileage between points served for mail.

The average daily designated mileage shall include the mileages of all scheduled trips designated or ordered to be established by the Postmaster General for the carriage of mail, and shall be computed as though the mileage of each such trip were the airport-to-airport distance via all certified intermediate points along the flight route between the terminals of each trip. The average daily designated mileage for each calendar month shall be determined by taking the average (computed to the nearest mile) of the daily mileages of regularly scheduled trips for the seven days of the week, without regard to any variations of scheduled mileage on holidays;

398 IT IS FURTHER ORDERED, That the aforesaid order fixing fair and reasonable temporary rates shall be effective as of this date, all parties to the above entitled proceeding having already waived all further procedural requirements short of a final decision by the Board fixing a temporary rate herein;

IT IS FURTHER ORDERED, That this proceeding remain open pending entry herein of an order fixing a final rate retroactive to such date as the Board shall then determine, which said final rate may be lower or higher than the temporary rate fixed herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

[Seal]

CRITERIA OF COMPARABILITY BASED ON THE TWELVE-MONTH
PERIOD ENDED DECEMBER 31, 1946

| Petitioner | Total Daily Non-Mail Revenue ¹ | Route Miles in Operation | Daily Non- Mail Rev. per Route Mile ¹ | Av. Daily Round Trip Frequencies | Av. Length of Pass. Haul | Perform- ance Factor |
|--------------------|---|--------------------------------|--|--|--------------------------------|----------------------------|
| Western | \$26,909 | 2,569 ³ | \$10.57 | 4.6 | 399.6 | 96.5% |
| Other 60c Carriers | | | | | | |
| Braniff | 27,443 | 3,658 | 7.50 | 4.3 | 397.4 | 98.1 |
| Chicago & Southern | 19,134 | 2,060 | 9.29 | 5.4 | 393.5 | 96.3 |
| Delta | 26,895 | 3,060 | 8.80 | 5.0 | 411.6 | 96.5 |
| National | 23,980 | 2,404 ² | 10.05 | 5.2 | 590.8 | 94.6 |
| Northwest | 50,331 | 3,338 | 15.01 | 7.6 | 604.2 | 96.5 |
| Penn.-Central | 48,709 | 3,379 | 14.50 | 7.2 | 278.0 | 93.8 |
| Need Rate Carriers | | | | | | |
| Colonial | 7,907 | 881 ⁴ | 9.15 | 4.9 | 295.3 | 89.9 |
| Continental | 10,697 | 2,794 | 3.84 | 2.7 | 369.6 | 97.3 |
| Inland | 3,125 | 1,194 | 2.62 | 2.3 | 275.0 | 96.7 |
| Mid-Continent | 10,750 | 2,293 | 4.92 | 3.2 | 302.7 | 97.7 |
| Northeast | 12,020 | 1,185 | 10.42 | 4.8 | 201.0 | 82.5 |

¹ For the eleven-month period ended November 30, 1946; Financial data for December 1946 not available for all carriers included in this analysis.

² As of December 31, 1946 the route mileage was 2587.

³ As of December 31, 1946 the route mileage was 2830.

⁴ As of December 31, 1946 the route mileage was 1062.

Source: C.A.B. Recurrent Reports of Traffic and Financial Data.

APPENDIX NO. 2

COMPARISON OF OPERATING RESULTS OF 60-CENT MAIL RATE
CARRIERS FOR THE CALENDAR YEAR 1945 AND BY QUARTERS FOR
THE CALENDAR YEAR 1946

| | Av. Daily Round Trip Fre- quencies | Av. Avail. Seats per Rev. Plane Mile | Av. Daily Available Seats per Route Mile | Av. Daily Rev. Pass. per Route Mile | Revenue Pas- senger Load Factor | Av. Daily Non-Mail Rev. per Route Mile | Total Cost per Avail- able Seat Mile | Total Cost per Rev. Pass. Mile |
|---------------------------------|--|--|--|---|---|--|--|--|
| Western | | | | | | | | |
| 1945—Year | 4.27 | 20.50 | 175 | 153 | 87.05% | 8.43 | 5.05c | 5.80c |
| 1946—Jan.-March | 5.39 | 22.76 | 235 | 187 | 79.38 | 9.38 | 4.96 | 6.25 |
| April-June ¹ | 4.12 | 27.80 | 229 | 180 | 78.78 | 9.15 | 4.77 | 6.03 |
| July-Sept. | 4.57 | 34.88 | 317 | 248 | 78.61 | 12.58 | 3.69 | 4.68 |
| Oct.-Dec. | 4.56 | 36.57 | 333 | 195 | 58.44 | 10.77 ³ | 3.79 ³ | 5.54 ³ |
| 1946—Year | 4.59 | 30.96 | 283 | 204 | 73.80 | 10.57 ⁴ | 4.14 ⁴ | 5.62 ⁴ |
| Other 60c Carriers ² | | | | | | | | |
| 1945—Year | 4.46 | 19.29 | 173 | 147 | 85.37 | 7.75 | 4.42 | 5.18 |
| 1946—Jan.-March | 4.90 | 20.10 | 198 | 163 | 83.69 | 7.91 | 4.87 | 5.84 |
| April-June | 5.77 | 24.39 | 285 | 233 | 82.21 | 11.23 | 3.95 | 4.81 |
| July-Sept. | 6.33 | 28.25 | 360 | 269 | 74.08 | 12.86 | 3.67 | 5.00 |
| Oct.-Dec. | 6.17 | 28.45 | 349 | 225 | 64.76 | 12.64 ³ | 4.01 ³ | 6.20 ³ |
| 1946—Year | 5.79 | 25.75 | 299 | 223 | 74.96 | 10.84 ⁴ | 4.00 ⁴ | 5.29 ⁴ |

¹ Operations on Route No. 68 begun April 1, 1946.² Simple average for Braniff, Chicago & Southern, Delta, National, Northwest and P.C.A.³ For the two months of October and November 1946. Data for December 1946 not available for all carriers included in this analysis.⁴ For the eleven-month period ended November 30, 1946.

Source: Derived from C.A.B. Recurrent Reports of Traffic and Financial Data.

(Filed Jan. 13, 1948)

403

BEFORE THE
CIVIL AERONAUTICS BOARD

Docket No. 1374

In the Matter of the Petition
of

WESTERN AIR LINES, INC. for an order fixing the fair and reasonable rates of compensation for the transportation of air mail over air mail Routes 13, 19, 52, 63 and 68.

Amendment No. 4.

TO THE HONORABLE, THE CIVIL AERONAUTICS BOARD:

1. On April 26, 1944, Applicant filed a petition with the Civil Aeronautics Board which was amended on February 10, 1947, February 24, 1947 and March 11, 1947 requesting the establishment over its entire domestic system of a permanent mail rate of 25 cents per airplane mile flown and a temporary emergency mail rate retroactive for such period and in such amount as the Board may deem appropriate, to serve as a provisional and immediate basis of payment pending the determination of a fair and reasonable final rate in this proceeding.

2. On April 29, 1947, the Civil Aeronautics Board issued its order No. E-484, fixing and determining the fair and reasonable temporary rate of compensation for the transportation of mail by aircraft pending the fixing of a final rate.

3. During the past year, Petitioner has reduced its total personnel by 867 or 36.2% and effected other substantial economies as well as twice increasing its passenger fares. However, inflation with its upward spiraling trend of prices has nullified the otherwise beneficial effect of these economies, and the rising cost trend is rapidly accelerating. Other

factors over which Petitioner has no control, such as foreign and domestic accidents and equipment grounding, have also adversely affected passenger revenues.

404 4. Petitioner hereby amends its petition in the above captioned proceeding in the following particular:

Paragraph 2 of Amendment No. 1 filed February 10, 1947 and which amended paragraph 9 of the original petition of April 26, 1944, is amended to read:

9. The fair and reasonable rate of compensation for the transportation of mail by aircraft, the facilities used and useful therefor and the services connected therewith as performed by Petitioner is the sum of thirty-eight cents (38¢) per airplane mile flown by Petitioner over its certificated routes, or the equivalent thereof based on such formula or method of calculation as may appear to be desirable or appropriate.

Such rate is needed by Petitioner as compensation for the transportation of mail and the services in connection therewith performed by it since the filing of this petition and to be performed hereafter

1. in order to insure the performance by Petitioner of such service as is required under the certificates of public convenience and necessity which Petitioner holds and under which it operates;

2. to insure the performance by Petitioner of such service as is required by the standards respecting the character and quality of service to be rendered as prescribed by or pursuant to law, and;

3. in order to enable Petitioner under honest, economical, and efficient management to maintain and continue the development of air transportation on its routes to the
405 extent and of the character and quality required by the commerce of the United States, the Postal Service and the National Defense.

WHEREFORE, Petitioner prays

(1) That a hearing be called and held as expeditiously as possible for the purpose of fixing and determining a permanent air mail rate for Petitioner in the amount alleged herein to be just and reasonable, or such greater amount as may be found by the Board to be just and reasonable under the circumstances, effective retroactively to the date of the filing of the Petition herein, and

(2) That such other, further and enlarged relief be accorded Petitioner as may by the Board be deemed justified in the light of the prevailing circumstances and the evidence submitted.

Respectfully submitted,

WESTERN AIR LINES, INC.

By Paul E. Sullivan

Guthrie, Darling & Shattuck
737 Pacific Mutual Building
Los Angeles, California

Served: Dec. 31, 1948

408

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 1374

WESTERN AIRLINES, INC.

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith.

Adopted: December 30, 1948.

Statement of Tentative Findings and Conclusions ¹

BY THE BOARD

Western Air Lines, Inc. (hereinafter referred to as Western) filed a petition on April 26, 1944 for an order fixing and determining the fair and reasonable rates for the transportation of mail over its routes. The petition was amended on February 10, February 24 and March 11, 1947, to request that the board set a rate of 25 cents per airplane mile effective May 1, 1944, and provide immediately for
409 a temporary rate. In response thereto, the Board on April 29, 1947, fixed and determined a temporary rate by Order No. E-484. On January 13, 1948, Western in a further amendment to its petition requested a rate of 38 cents per airplane mile.

In accordance with Section 285.13 of the Economic Regulations, the Board has arrived at the tentative findings and conclusions and has formulated the tentative mail rates set forth herein. Concurrently, the Board has issued an order directing Western to show cause why these tentative mail rates should not be established as the final rates in this proceeding.

¹ This Statement does not necessarily represent the view of all members of the Board with respect to all issues.

The following appendices are a part of this Statement :

| Particulars | Appendix No. |
|---|--------------|
| Traffic Statistics for the Past Period and as Estimated for a Future Year | 1 |
| Operating Results for the Past Period, as Reported and as Adjusted | 2 |
| Operating Results for a Future Year as Estimated by Western and as Adjusted | 3 |
| Operating Expenses per Revenue Ton-Mile and per Available Ton-Mile, as Reported and as Adjusted | 4 |
| Reported and Recognized Investment for the Period May 1, 1944 to December 31, 1948 | 5 |
| Estimated and Recognized Investment for a Future Period | 6 |
| Sliding Scale Mail Rates | 7 |

Present Mail Rate

A service rate of 60 cents per mail ton-mile was made effective for Western on January 1, 1943.² In response to the amended petition requesting a temporary rate, the 60-cent per ton-mile rate was modified,³ effective October 1, 410 1946, by applying it to mail ton-miles computed from minimum capacity loads, and related to a daily base mileage of 21,000 miles. The initial minimum capacity load was set at 700 pounds per airplane mile and was gradually reduced to 250 pounds, effective on and after July 1, 1948. The order establishing this temporary rate provided that the proceeding remain open pending the entry of an order fixing a final rate which would be retroactive to such date subsequent to the date Western first filed a petition as the Board should determine and might be lower or higher than the temporary rate. Simultaneously the Board issued an order⁴ instituting an investigation and requiring a special

² *Western A. L., Mail Rates* 4 C.A.B. 441 (1943).

³ Order Serial No. E-484 (April 29, 1947).

⁴ Docket No. 2911, Order Serial No. B-485 (April 29, 1947).

report from Western to determine what factors were responsible for the increasing dependence on the Government through need mail payments and in what manner this dependence could be decreased. The carrier submitted a report, and the investigation was carried out, the results of which, insofar as they pertained to need for mail pay, have been incorporated in these findings.

Routes Operated

Western holds certificates of public convenience and necessity authorizing it to engage in air transportation with respect to persons, property and mail between the following terminal points:

Route No.

- 13 San Diego, Calif., and Salt Lake City, Utah
- 19 Salt Lake City, Utah and Great Falls, Montana
- 52 Great Falls, Montana and Edmonton, Alberta, Canada.
- 63 Los Angeles, Calif., and Seattle, Washington

Western also holds a certificate of public convenience and necessity authorizing it to engage in air transportation with respect to persons, property, and mail between Los Angeles, California and Mexico City, Mexico. Service has not been inaugurated on this route nor on the extension of Route 52 from Lethbridge to Edmonton, Canada, pending approval of the respective foreign governments.

Periods For Which Rates Will Be Fixed

The initial petition in this proceeding was filed by Western on April 26, 1944. Accordingly, under section 406 of the Act, Western's mail rate for the period following that date is open for review. For approximately a year and a half following the filing of its petition Western earned a greater return on its investment under the service mail rate fixed by the Board on November 8, 1943, than the Board is currently

providing carriers for past periods. During this period, the petition, from the point of view of Western, was protective in nature, since the mail rate as established was more than adequate to provide a reasonable return. It would be more advantageous to Western, therefore, if, as Western has informally requested, the Board were only to revise Western's mail rate from January 1946, when it first started to incur significant losses, since such a review would not result in offsetting relatively high profits earned from April 1944 to January 1946 against losses suffered subsequently.

Recently, the Board's position that it has no legal power to make an adjustment of a mail rate prior to the date on which it is challenged has been attacked in court, with the result that the Board's position has been upheld by the U.S. Court of Appeals for the District of Columbia, but one of the cases is still pending before the Supreme Court.⁵ In these cases it was argued before the Board that failure to adjust rates retroactively would cause all carriers to keep

412 "protective" petitions on file with the board at all times.⁶ We indicated that we did not anticipate such a development, and pointed out that should a carrier file a petition and "thereafter earn more than a fair and reasonable return, our rate order, effective from date of filing, would effect a reduction in mail pay from that date forward." The present case falls squarely within that principle.

The effect of keeping the mail rate constantly in issue through the device of "protective" petitions, is to place the carrier on a cost plus basis. It would obviously be inequitable and contrary to the public interest to provide protection to the carrier against losses without reciprocal protection

⁵ *Transcontinental & Western Air, Inc. v. Civil Aeronautics Board*, 169 F. (2d) 893 (1948), Cert. granted (December 6, 1948); *Capital Airlines, Inc., v. Civil Aeronautics Board*,—F. (2d)—(App.D.C., December 6, 1948).

⁶ *Transcontinental & Western Air, Inc., Mail Rates*, Docket No. 2849, Order Serial No. 1033 (December 2, 1947); *Pennsylvania-Central Airlines Corp., Mail Rates*, Docket No. 484, Order Serial No. E-1032 (December 2, 1947).

to the Government against excess profits. Under all the circumstances, we find that it will effectuate the policies of the Act to make our rate order for Western effective from May 1, 1944, the approximate date of filing of the initial petition.

By the end of 1948, or shortly thereafter, Western will have substituted Convair 240 aircraft for its DC-4 equipment and a large part of its DC-3 equipment. Since a marked change in the character of its operations will result from the equipment changeover, we shall fix a fair and reasonable mail rate for the past period from May 1, 1944, up to and including December 31, 1948, and fix a separate future rate from January 1, 1949. Our determination of the rate for the past period will be based upon results on file with the Board for the period since May 1, 1944, and estimates filed by the carrier for the last few months of 1948.

**MAIL RATE FOR THE PERIOD MAY 1, 1944
TO DECEMBER 31, 1948**

Nature of Operations in Past Period

During the first half of the period under review, Western's operations were for the most part directly affected by the war-time demand for transportation. Approximately two-thirds of Western's fleet of 12 DC-3's and Lodestars had been transferred to the Government, leaving only five DC-3 aircraft to service its routes. As a result of the limited number of seats available during a period of unprecedented demand for air transportation, the passenger load factor for the last eight months of 1944, which mark the beginning of the review period, was 91 percent, and for the year 1945, 89 percent.

Beginning May 1, 1944, and during the remainder of 1944, extensive changes occurred in Western's operations. On that date, service was inaugurated on Route 63 from Los Angeles to San Francisco, destined to be the segment with the highest frequencies and the greatest revenue yield of

the system. By June 1, 1944, the purchase of the majority interest in Inland Air Lines was consummated. Inland was gradually integrated into Western's system to a point where Western's management and facilities were employed in the operation of Inland to the same extent as for Western. During the year 1944, Western was also awarded Route 68 with terminal points at Los Angeles and Denver, on which operations were not inaugurated until April 1, 1946.

At the end of 1945, the carrier inaugurated operations on the extension of Route 13 into the Imperial Valley via Palm Springs and Yuma. Also stops at Cedar City, Logan, and Jackson were added to Routes 13 and 19 in 1946. On April

1, 1946, operations were begun on Route 68 to Denver
414 with an initial frequency of one round trip per day.

As soon as equipment was available, frequencies were increased to four round-trips, which Western maintained until the time when it was preparing to transfer the route to United. Load factors were relatively high on this route, and passenger traffic accounted for approximately 29 percent of annual volume during the nine months of operation in 1946 and eight and a half months in 1947. Operations over Route 68 were conducted until September 15, 1947, when, after approval by the Board, the route certificate together with DC-4 flight equipment and ground equipment pertaining to the route were sold to United Air Lines for the sum of \$3,750,000.¹ This action resulted from the decision of Western's management to withdraw from competition for transcontinental traffic and to confine itself to development of regional operations.

On August 1, 1947, a short time prior to the transfer of Route 68, operations were inaugurated on the extension of Route 63 from San Francisco to Seattle. Round-trip frequencies on the Denver route were reduced from four to two in July, to provide equipment and personnel for the new service to Seattle, which was inaugurated with three round-

¹ *United-Western, Acquisition Air Carrier Property*, 8 C.A.B. 298 (1947).

trip frequencies. Although the transfer of operations resulted in no large variance in route miles, competition was much greater on the coastal route where United had operated exclusively for a long period, and Western experienced load factors during the first year or more considerably below those realized on Route 68.

Western has been certificated by the Board to operate two additional routes: an extension of Route 52 from Lethbridge to Edmonton, Canada, and a route from Los Angeles to Mexico City via La Paz. Inauguration of services has been

415 delayed pending approval of the respective foreign governments. The operation of the Route 52 extension to Edmonton will be considered part of the domestic system and as such will be covered by the mail rates here established or as hereinafter revised when service is ultimately inaugurated. Mail rates for the route to Mexico City will be established in a separate proceeding after operations are inaugurated on that route. At the end of 1948, Western's route structure had been stabilized except for the possible transfer to Arizona Airways of part of Route 13, extending from San Diego to Yuma, application for which is now pending before the Board.

Scheduled Services Required

We have included in Appendix No. 1 a summary of the significant traffic data for the past and future periods.

During the period under review, Western's volume of operations expanded at a rapid pace, largely influenced by the inaugurations of operations on Route 68 on April 1, 1946. Available seat miles increased 365 percent from the last six months period of 1944 to the same period of 1946. At the same time passenger miles increased 250 percent to 115,339,000. The level of operations was also high in the first half of 1947, although the passenger load factor had dropped 17 percentage points from the same period a year earlier when traffic was still influenced by the war-time demand for transportation. The sale of Route 68 in September 1947, along with an overall decline in air travel, was accompanied by a substantial decline in passenger miles, so

that in the last half of 1948, Western carried only about 50 percent as many passenger miles as during the last half of 1946 when its traffic volume reached the peak. The sharp expansion and contraction in volume of operations is readily apparent from the following table.

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Volume of Operations
1944-1948
(000)

| Six Month Period Ended | Revenue Plane Miles | Available Seat Miles | Revenue Passenger Miles | Passenger Load Factor |
|---------------------------|------------------------|-------------------------|-------------------------------|-----------------------------|
| December 31, 1944 | 1,842 | 36,621 | 32,960 | 90% |
| June 30, 1945 | 2,303 | 46,518 | 40,207 | 86 |
| December 31, 1945 | 2,983 | 61,872 | 54,150 | 88 |
| June 30, 1946 | 3,863 | 96,667 | 76,321 | 79 |
| December 31, 1946 | 4,719 | 169,010 | 115,339 | 68 |
| June 30, 1947 | 3,752 | 141,143 | 87,846 | 62 |
| December 31, 1947 | 3,602 | 127,303 | 78,550 | 62 |
| June 30, 1948 | 3,041 | 93,904 | 51,474 | 55 |
| December 31, 1948 | 3,274 | 103,822 | 57,831 | 55 |

Despite the increase in volume of services, Western was able to maintain passenger load factors which have been consistently above the average of intermediate group carriers. The table below indicates only one twelve month period in which Western was below the average of the group of carriers with which it is compared. For the twelve months ended September 30, 1948, Western was two percentage points above the group average, even though the average for the year 1948 is estimated at 55 percent.

Passenger Load Factors
of Intermediate Group Carriers

| | Twelve Month Periods Ended | | | |
|------------------------------------|----------------------------|----------|----------|---------|
| | 12-31-45 | 12-31-46 | 12-31-47 | 9-30-48 |
| Average of 5 Carriers [*] | 84% | 73% | 57% | 53% |
| Western | 87% | 72% | 62% | 55% |

^{*} Five carriers are Braniff, Capital, Chicago & Southern, Delta, and National. National is omitted from twelve months ended 9-30-48 because of distorting effects of Strike.

Average daily round-trip frequencies operated by Western ranged from a low of 2.8 round trips for the last

eight months of 1944 to a high of 5 round trips in 1946. Operations for the recent route pattern have been stabilized at 3.2 round trips for 1948 with the same frequencies estimated for the future years. The following table shows the round-trip frequency and load factor for major route segments in 1948.

| Segment | 1948 | |
|-------------------------------|------------------------------|-----------------------|
| | Average Round-Trip Frequency | Passenger Load Factor |
| Los Angeles—San Francisco | 7.8 | 60.5% |
| San Francisco—Seattle | 3.0 | 43.7 |
| Los Angeles—San Diego | 4.0 | 60.4 |
| San Diego—Yuma | 0.5* | 38.3 |
| Los Angeles—Salt Lake City | 3.3 | 65.4 |
| Salt Lake City—Great Falls | 2.0 | 58.2 |
| Great Falls—Lethbridge System | 1.0 | 45.5 |
| | <hr/> 3.2 | <hr/> 55.1% |

* Three days a week only.

It will be noted that all segments with frequencies over two round trips had load factors over 60 percent except the San Francisco—Seattle segment, which was only placed in operation in August 1947, and was still in the development stage in 1948. If this segment were eliminated from the computation, the system load factor would be approximately 60 percent for the year.

Upon consideration of the foregoing, we find that all the scheduled services operated during the past period from May 1, 1944 to December 31, 1948, were reasonably required in the interests of one or more objectives of the Act.

Equipment

At the beginning of the review period Western was operating five DC-3 aircraft, having given up a major portion of its fleet of DC-3's and Lodestars to the armed services during the war. By the end of 1945, twelve DC-3's were in operation. The DC-3 fleet was augmented in

early 1946 by one passenger and two cargo aircraft. The cargo equipment was used primarily in the DC-4 pilot training program and the training was spread fairly evenly over the first nine months of the year. Approximately 2200 hours were flown by the two cargo aircraft in 1946, all in non-revenue service, resulting in an average daily utilization of less than three hours each. The amount of training on DC-3 aircraft in any one month does not appear to have warranted the use of more than one training plane, in addition to time available from one spare passenger plane and turnaround time of passenger equipment at terminal points. We find therefore that one DC-3 cargo aircraft was in excess of Western's needs for the performance of scheduled services required from the date placed in service until its conversion for use in scheduled passenger service in July 1947.

Beginning in 1946, Western instituted a procedure of allocating depreciation on DC-3 aircraft to Inland on the basis of hours flown by Western's aircraft on Inland's routes. Prior to 1946, Inland paid rental for the use of this equipment. For the years 1946 through 1948 Inland used an average of three of Western's DC-3's. Western owned a spare aircraft throughout the period, which was used primarily for a maintenance spare. It is appropriate therefore to pro-rate this spare on the basis of the ratio of equipment used by the two companies. Accordingly, we consider that a total of 3.25 of Western's DC-3's was attributable to Inland's operations, and we have used this factor in our computations of allocated expense and investment herein.

419 In 1946, Western received and placed in service 13

DC-4 aircraft, being one of the first domestic carriers to operate this equipment on its routes. These aircraft were used to operate Route 68 to Denver, on which service was inaugurated April 1, 1946, and the coastal routes. Following the rapid drop in traffic volume which began in the fall of 1946 and extended into 1947, Western moved quickly to

reduce its DC-4 fleet by selling three DC-4's over the period from November 1946 to July 1947, from which sales substantial profits were realized. Western had purchased one C-54 cargo plane for transition training to DC-4 equipment, but it was not placed in service until October 1946, when most of the training had been completed. Since this aircraft was not required for scheduled service, we have disallowed it as excess equipment.

In equipping for DC-4 operations, Western overestimated its requirements for spare engines, and as a result owned 92 R-2000 engines at the end of 1946, which provided over 100 percent spare coverage for installed engines. This situation extended throughout most of 1947. We have considered therefore that an average of 15 R-2000 engines were in excess of the carrier's requirements from July 1, 1946 through December 31, 1947.

As early as 1945, Western had placed an order for ten Convair 240 aircraft, being one of the first two domestic carriers to contract for this equipment. Deliveries were not commenced, however, until June 1948, and the first three Convairs were placed in service on September 1, 1948.

420 Shortly after the end of the review period, the carrier plans to have all of its Convairs in operation, replacing five DC-3 and five DC-4 aircraft according to the following schedule:

| As of First of Month | Total Convairs in Operation | Equipment Retired | |
|-------------------------|--------------------------------|-------------------|------|
| | | DC-3 | DC-4 |
| September 1948 | 3 | 2 | 1 |
| October 1948 | 5 | 2 | 1 |
| November 1948 | 5 | 0 | 0 |
| December 1948 | 7 | 1 | 2 |
| January 1949 | 10 | 0 | 1 |

Western began receiving delivery on spare parts and engines for the Convair fleet in 1947 and early 1948, although the first aircraft were not to be placed in service until later in the year. In accordance with previous Board policy in such matters, we have disallowed this equipment as used

and useful in scheduled operations until such time as the new aircraft are placed in service. We have allowed the carrier to capitalize interest on the amount of such equipment in the same manner as for equipment purchase funds. This procedure is discussed in greater detail in a following section.

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Non-Mail Revenues

The non-mail revenues for the past period have been set forth in Appendix 2, attached hereto, together with explanations of adjustments which have been made for rate making purposes.

In 1944 and 1945, Western had an equipment rental agreement with Inland for the use of Stinson, Lodestar, and DC-3 aircraft owned and maintained by Western. After 1945, Western received approval for the allocation of aircraft operating expenses to Inland, which replaced the procedure of rental payments by Inland. Since the Stinson and Lodestar were disallowed as operating equipment for Western, as well as all costs for maintenance and depreciation, it is necessary that these costs be offset against the rental revenues received from Inland. Accordingly, we have reduced incidental revenues in the amounts of \$32,000 and \$72,000 for 1944 and 1945, respectively.

A similar situation existed in 1947, when Western rented its DC-4 cargo aircraft to United Air Lines for the last six months of the year. We have disallowed this aircraft as excessive equipment for the operation of the scheduled services required, but have included in incidental revenues the rental revenues received from United. We find it proper, therefore, to offset against these revenues the amount of depreciation and insurance expense which Western incurred for this DC-4 in 1947. Accordingly, we have reduced incidental revenues of \$323,000 for the year 1947 by \$54,000 representing expense incurred during the period the cargo DC-4 was rented to United, and have included the balance of \$269,000 in non-mail revenues.

In 1948, actual non-mail revenues have been included for the first nine months through September 30, and we have accepted the carriers estimate for the last quarter. Western increased passenger fares 10 percent on September 1, 422 1948, at which time a general fare increase was instituted by the industry. At the same time, a 5% round-trip discount was provided, resulting in an estimated effective fare increase of 8% for the last four months of 1948. The average yield per passenger mile was raised from 5.60 cents to approximately 6.04 cents as a result of the increase.

Other revenues for 1948 totaled \$286,000, of which \$206,000 represented incidental revenues and approximately \$80,000 charter revenues. Incidental revenues of Western are greatly in excess of comparable carriers, because of the large amount of services provided for others. These revenues were 4.23% of non-mail revenues for the nine months ended September 30, 1948, compared to an average of 1.0% for four carriers in the intermediate group.⁹ The principal reason for the high revenues was the failure to report only the excess of fees and charges over costs incurred as provided for in the Uniform System of Accounts. These costs, estimated by Western at \$186,000, have been reported under operating expenses. It is proper therefore that this amount of incidental revenues be offset by an equal amount of operating expenses, and we will adjust operating expenses accordingly.

Adjusted over-all non-mail revenues for 1948 are \$6,670,000, a decrease of 28% from the \$9,241,000 received in 1947, resulting largely from the elimination of the traffic generated by Route 68.

We have included in non-mail revenues for the past period the amount of \$131,247 of incidental revenues representing revenues from the operation of restaurants and food service at airports served by Western. The carrier 423 claims that the net profit reported consisted entirely of profit from coin vending and slot machines

⁹ The carriers are Braniff, Capital, C&S, and Delta.

located on the restaurant premises, and as such cannot reasonably be included in non-mail revenues for the determination of need for mail pay. This position is inconsistent, however, with established Board policy with respect to incidental revenues as set forth in past rate cases.¹⁰

Total non-mail revenues for the past period are therefore \$33,216,000, equal to 110.90 cents per revenue plane mile.

Property Retirement Income

In 1946 and 1947, excess DC-4 aircraft were sold for a substantial profit. After taking into account the losses on retirement of operating property in those years, the carrier realized a net gain of \$149,000. Losses on retirement were incurred, however, amounting to \$4,000 in 1944 and 424 \$29,000 for the first nine months of 1948 which we will allow the carrier to offset against the gain. We have therefore taken into account as "other revenue" in determined mail pay need the net gain of \$116,000 applicable to the entire period.

Sale of Route 68

On September 15, 1947, after approval by the Board,¹¹ Western sold to United Air Lines its certificate for Route 68, with terminal points at Los Angeles and Denver, together with four DC-4 aircraft, certain spare parts, certain ground and station equipment, and miscellaneous supplies. The tangible property transferred by Western was valued at \$1,528,000. The total price paid to Western by United was \$3,750,000. After charges of approximately \$98,000, consisting of the cost of cancelling DC-6 purchase commitments and miscellaneous expenses connected with the sale, Western reported a net profit before taxes on the transaction of \$2,123,917.

¹⁰ *Chicago and Southern Air Lines, Inc., Mail Rates*, 3 C.A.B. 161 (1941). *TWA Mail Rates*, 2 C.A.B. 226 (1940).

¹¹ *United-Western, Acquisition Air Carrier Property*, 8 C.A.B. 298 (1947).

Section 406 (b) of the Act provides that in fixing fair and reasonable mail rates the Board shall consider the "need" of the air carrier for compensation which, "together with all other revenue," will enable it to achieve the statutory objectives. Western realized a profit on its transaction with United. The profit arose from the sale of flight and other equipment and supplies and the certificate for Route 68, which together constituted a portion of Western's going business. We find that the proceeds of the sale constituted "other revenue," within the meaning of section 406 (b) of the Act. Accordingly, the proceeds of the sale will
 425 serve to reduce Western's "need" for mail compensation. The amount by which Western's "need" for mail pay will be reduced remains to be considered.

Prior to the sale, Western operated the route for about 18 months. During the first nine months of operation of Route 68, from April 1 to December 31, 1946, Western realized a profit of \$640,000 therefrom. During the year ended March 31, 1947, 27 percent of the passengers carried by Western on Route 68 were exchanged with United at Denver and traveled to or from Chicago and points east thereof.¹²

Western incurred certain extraordinary costs in connection with the establishment, operation and disposition of Route 68. But for the expenditure of these sums it would have been unable, in large measure, to realize the profit it did upon the sale of the route. We believe it proper, therefore, to charge these expenditures against the profit realized on the sale of Route 68 in determining the amount of "other revenue," within the meaning of section 406 (b) of the Act, which Western received and which reduced Western's "need" for mail pay.

In establishing the route Western incurred preoperating and training costs, including depreciation on flight training equipment, and extension and development costs. In order to avoid distortion of Western's costs during the period

¹² Id., pp. 301-302.

when the expenditures were made, these costs would ordinarily be capitalized and spread over a reasonable period of years. Since, however, Western has sold Route 68, which alone benefited from such expenditures, we find it appropriate to charge the unamortized portion of such expenditures to the profit otherwise realized on the sale.

Likewise, Western incurred abnormal maintenance costs during the period Route 68 was operated as a part of its system. These high costs were incurred largely because the addition of Route 68 to Western's system greatly overburdened its facilities. Nevertheless, the early addition of Route 68 gave rise to operating profits and to the profit upon the sale of the route, which reduced Western's "need" for mail pay. Under these circumstances, it is appropriate to charge the abnormal maintenance costs against the profit realized on the sale of the route, to the extent that such abnormal costs had their incidence in relation to the expanded operations of Route 68.

Finally, Western incurred certain costs after the sale of Route 68 as a result of its inability immediately to curtail its operating expenses to fit its reduced volume of operations. The sale of the route reduced Western's operations approximately 29 percent, just as its inauguration substantially increased its volume. It is recognized that some period of time must necessarily elapse before costs can be cut to meet sharply reduced volume. In part, the profit to Western on the sale of the route is a recognition of the continuing nature of certain operating expenses beyond the date of disposition of the route. We find that these continuing expenses, which we shall term "divestment costs," should be charged to the profit on the sale of the route.

We shall discuss these adjustments to the profit on the sale of the route below. They may be summarized as follows:

| | |
|---------------------------|-------------|
| Profit realized from sale | \$2,124,000 |
|---------------------------|-------------|

Charges Against Profit

| | |
|---|---------|
| Unamortized balance of pre-operating and training costs | 123,000 |
| Unamortized balance of extension and development costs | 26,000 |
| Depreciation on flight training equipment | 85,000 |
| Abnormal maintenance costs directly related to Route 68 | 170,000 |
| Abnormal loss estimated on retirement of DC-4 non-rotatable spare parts | 145,000 |
| Divestment costs | 781,000 |

\$1,330,000

Net profit from sale included as "other revenue" \$794,000

On the basis of the foregoing, we shall consider the sum of \$794,000 as the net "other revenue" to Western from the sale of Route 68. Accordingly, we find that the mail pay which Western "needs" for the past period is reduced by that amount.

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Operating Expenses

Recognized operating expenses and the adjustments we have made thereto for rate-making purposes are shown in Appendix No. 2. As a result of these adjustments reported operating expenses and the carrier's estimates for the last six months of 1948, amounting to \$39,339,000, have been reduced to a total of \$36,405,000, equal to 121.54 cents per revenue plane mile. A detailed explanation of the adjustments follows.

Flying Operations

The total adjustment for flying operations expense for the past period is \$131,000. The greater part of this amount represents training cost of \$88,000 incurred in 1946 for transition pilot training for DC-4 equipment, most of which was

operated on Route 68. This amount was capitalized along with other training costs as of April 1, 1946, the date service was inaugurated on the new route, and amortized over a five-year period. The unamortized portion at September 15, 1947, the date of the route sale to United, was charged against the profit received from the sale since the amortization was applicable to the operation of that particular route. The remainder of the adjustment, amounting to \$41,000, represents excess of Western's estimate over our allowance for the last six months of 1948. We have based our estimates on the actual experience for the first six months of 1948, which results in costs for the DC-3 and DC-4 of \$38.61 and \$66.73, respectively, per hour flown. The carrier has not provided any reasonable basis for higher costs in the last half of 1948, and we have accordingly not recognized the amount of \$41,000 in excess of our allowance.

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Direct Maintenance—Flight Equipment

Adjustments to direct maintenance expenses total \$762,000 for the period. A large part of this total, however, represents elimination of reserve accruals or expense which is charged against the profit on the sale of Route 68.

In 1946, when operations were expanded on a large scale and service on Route 68 was inaugurated, total DC-3 direct and indirect maintenance expense increased significantly, reaching a total of \$38.24 per hour in 1946, and \$36.52 per hour in 1947. These costs were 48 percent above the industry average of \$25.81 in 1946, and 37 percent above the industry average of \$26.64 in 1947.

The carrier claims that high maintenance costs were due to a number of reasons, the one most capable of measurement being the shorter overhaul periods than the average for the industry. Other reasons advanced by the carrier which are not as susceptible of exact measurement are as follows: (1) the inadequacy of facilities at the maintenance base at Burbank, California, where maintenance operations for approximately 25 aircraft owned at the end of 1946 were

carried on in an area that was hardly sufficient for the war-time fleet of five DC-3's; (2) the necessity for engaging an outside contractor to perform engine overhauls because of lack of shop space to set up its own overhaul shop; and (3) the relative inefficiency of personnel because of the rapid expansion of operations and the inefficient arrangement of maintenance facilities. We find that the carrier did make an attempt to obtain space at the Lockheed Air Terminal in order to establish its own engine overhaul shop just prior to the war, and that plans had to be postponed because of the need for all available space at the terminal for the armed services. Consequently, during the war period and throughout the period under review the carrier has farmed out all

engine overhauls. It is clear that some added costs
430 were incurred due to the necessity of maintaining a separate stock room, of paying a handling charge on parts furnished, and of paying for overhead and profit of the contractor. The carrier took action to remedy this situation by planning in 1945 to construct a modern hangar at the Los Angeles Municipal Airport. The hangar was completed and maintenance activities were transferred to Los Angeles in the middle of 1947 thus relieving the overcrowded conditions at Burbank. The engine overhaul shop is expected to be completed and in operation by the end of 1948, effecting a saving on overhauls estimated by the carrier at 25 percent.

It appears that the difficulties encountered at the Burbank base were compounded by the addition of DC-4 aircraft to the fleet, principally for the operation of Route 68. It became necessary for the carrier to maintain mechanics at Salt Lake City and San Francisco to perform inspections and routine maintenance on DC-3's during layover time at those points. Maintenance expense for DC-4 aircraft does not appear to be unreasonably high, however, in comparison with other DC-4 operators, due in part to the absence of necessity for performing overhauls on the DC-4's even though Western was accruing a reserve for this purpose.

This fact decreases the significance of the contentions relative to the inadequacies of the maintenance plant.

Western claims that the length of its overhaul periods prescribed by CAA operation specifications for various components of DC-3 aircraft and engines is considerably shorter than for most other domestic operators and has presented comparative data for six domestic carriers which it feels are representative of the industry i.e., Braniff, Chicago & Southern, Continental, Delta, Northeast, and Northwest. In comparison with Delta, which operates mostly in the southeast, Western's engine changes were 25 percent more frequent, the reason for which is claimed to be the longer periods of engine operation at high power setting during climbs to minimum operating altitudes. In
 431 addition, during most of the review period, inspections were performed by Western either daily or every 35 hours, whereas most of the other carriers performed inspections at less frequent intervals. Check periods for major DC-3 and DC-4 aircraft and engine assemblies were usually more frequent for Western than for the other carriers in the comparison except Northeast, which had approximately the same inspection and check periods as Western. Although length of overhaul periods and frequency of maintenance checks are governed to large extent by the efficiency of the carrier based on past experience, it appears that in this instance the predominating factor was the hazardous terrain over which the carrier operated, particularly with respect to DC-3 aircraft.

In view of the foregoing considerations and recognizing the impracticability of measuring the influence of the above factors in terms of specific costs, we believe that an allowance of approximately 15 percent above the average of the industry will reasonably compensate the carrier for the shorter overhaul periods due to circumstances beyond management control, for higher engine overhaul costs incurred by the necessity of contracting for engine overhauls outside of its own shop, and to a limited extent only for the inade-

quate facilities available for maintenance activities. On this basis, the average allowance for DC-3 direct and indirect maintenance expense for the years 1946 and 1947 is \$30.00 per hour flown. Expenses incurred by the carrier above this figure are believed to have been subject to management control to such an extent as to warrant their exclusion from operating expenses recognized for rate-making purposes. The disallowance amounts to \$291,000 in 1946, and \$161,000 in 1947, applicable to direct maintenance expense in those years.

Direct flying costs incurred for pilot training in 1946 included \$38,000 of direct maintenance expense. This amount has been eliminated from reported expense and capitalized as of April 1, 1946, along with flying operations expense, making a total of \$126,000 direct flying cost capitalized.

As we indicated above in the case of flying operations expense, the carrier estimated expenses for the last half of 1948 which varied from the costs used herein, based on actual experience for the first half of the year, by \$65,816. We have accordingly not recognized this expense in 1948.

Western has followed the practice of accruing aircraft and engine overhaul reserves during the past period. As we have stated in previous decisions,¹³ however, the concurrent accrual of overhaul and depreciation reserves from the date aircraft are placed in service tends to burden current operations with costs which are greater than those actually incurred. Since the benefits of a major overhaul will accrue to a carrier subsequent to the overhaul, when the restored life will be used, that part of the original cost which is the value of the "built-in" overhaul should be amortized over the hours remaining to the next overhaul by charges to maintenance expense, while the remainder of the original cost in excess of the residual value should be depreciated

¹³ *Southwest Airways Company, Mail Rates*, Docket No. 2653, Order Serial No. E-1478 (April 27, 1948).

American Overseas Airlines, Inc. Mail Rates, Docket No. 1666, Order Serial No. E-2247 (November 29, 1948).

over the service life of the equipment to provide recovery of that value not related to overhaul. In accordance with this principle, we have eliminated DC-3 aircraft overhaul expense as charged by the carrier and allowed the amortization of the cost of the "built-in" overhaul and of each subsequent overhaul over a two and a half year period, the average length of time between overhauls. In the instant case this adjustment results in a net disallowance of \$2,197 in the past period, which amount has been allowed as amortization in the future period.

433 Because we are allowing amortization of overhaul expense after the performance of the overhaul, we have adjusted the overhaul reserve account at the close of the past period. For DC-3 aircraft, this adjustment amounted to \$64,000. Western has not performed any overhauls on the DC-4's, nor are any anticipated before the aircraft are retired at the end of 1948. The carrier accrued depreciation on the total amount of the original cost less 10 percent residual value, without a reduction for the value of the "built-in" overhaul. We estimate that DC-4 depreciation reserves at the actual date of retirement of the equipment should be sufficient to insure against the likelihood of any appreciable gain or loss on retirement. Under these circumstances, we shall not adjust for "built-in" overhaul and shall eliminate accruals to the reserve for DC-4 aircraft overhauls in the amount of \$80,000.

We have not provided for the amortization of engine overhaul costs subsequent to the overhaul for practical reasons, since the overhaul period on an engine is usually shorter than the annual accounting period, and the average amount of amortization would not extend into another period so as to distort the results for rate-making purposes.

The carrier reported direct maintenance expense on the Lodestar and Stinson which it owned in 1944 and 1945 but which were rented to Inland during this period. As we indicated above in discussing incidental revenues, we have allowed the amount of direct flying costs incurred by Western

during the period through December 1945, as an offset against incidental revenues. Accordingly, we have eliminated the amount of \$61,000 from maintenance expense.

Route 68 Developmental Expense

We have indicated in our discussion of maintenance expense that Western incurred certain costs which were unreasonably high, due in part to the addition of Route 68 operations with DC-4 aircraft to a maintenance plant which
434 was already inadequate for DC-3 maintenance. It appears improbable that the excess in costs would have been as great if the route had never been placed in operation, for the route was sold in September, 1947, and results for the year 1948 indicate that DC-3 maintenance expenses will be below the \$30.00 per hour which we have allowed for 1946 and 1947. Consequently, a large portion of the excessive costs may be considered directly attributable to Route 68. It is appropriate, therefore, in view of the reduction in expense level after the sale of the route, to consider one-half of the total excess direct maintenance expense incident to the operation of Route 68.

We have allowed Western to capitalize the amount of \$226,000 and to amortize this amount over a five-year period. Approximately \$145,000, representing one-half of the disallowance in 1946, has been amortized from April 1, 1946, the date service was inaugurated on Route 68, and \$81,000, or one-half of the 1947 disallowance has been amortized from January 1, 1947. At the time of the sale of the route on September 15, 1947, the unamortized balance of development expense was \$170,000, which has been applied as an offset to the reported profit from the sale.

DC-3 Depreciation

Western had depreciated all owned and leased DC-3 aircraft to a 5 percent residual value at December 31, 1947, except for one passenger and one cargo aircraft, which were depreciated over a service life to December 31, 1948. En-

gines were depreciated over a service life to December 31, 1947.

In accordance with the Board policy set forth in recent cases ¹⁴ we have established a common retirement date of June 30, 1949, for all DC-3 flight equipment, and a uniform residual value on owned equipment of \$5,000 per aircraft and \$500 per engine. The recomputation of depreciation expense on the above basis from May 1, 1944, the approximate date of petition, resulted in a disallowance of expense in the past period of \$225,000, of which \$142,000 has been allowed in the future period, leaving a net disallowance due to the extension of the service life of \$83,000. The major part of this adjustment is the result of retirement of three aircraft in 1946 due to accidents, the allocation of depreciation to Inland subsequent to the filing of a petition by that carrier on March 28, 1947, and substitution of Convair 240's for five DC-3's in 1948.

Beginning in January 1946, depreciation expense had been allocated to Inland on the basis of hours flown by type of equipment. The amount so allocated was equivalent to depreciation on approximately three aircraft. Because of the joint use of equipment between the two companies and the necessity of Western having a maintenance spare, it is believed appropriate to allocate a portion of this spare DC-3 to Inland on the basis of the ratio of Western's equipment used by Inland to the total number of passenger aircraft. We have added one fourth of Western's spare to the three aircraft regularly used by Inland for a total of 3.25 aircraft and have allocated depreciation on all DC-3 flight equipment on this basis for the years 1946 and 1947 and the first eight months of 1948. After September 1, 1948, when Western began to retire five DC-3's during the period to December 1, 1948, the proportion of allocable depreciation expense to Inland was revised upward to reflect the increased ratio of DC-3's used on the Inland routes.

¹⁴ *Braniff Airways, Inc. Mail Rates*, Docket No. 2680, Order Serial No. E-2129 (October 28, 1948); *Delta Air Lines, Inc. Mail Rates*, Docket No. 3119, Order Serial No. E-2130 (October 20, 1948).

Since Inland's petition was not filed until March 28, 1947, we have made no change in the amount of depreciation already allocated to Inland prior to that date. Although the spreading of depreciation forward to June 30, 1949, 436 had the effect of decreasing the amount of allowable depreciation expense in 1946, the increase in the ratio of allocation to Inland, tended to offset the amount of the decrease, so that the net effect was negligible.

As we have indicated previously, the net book value of the DC-3 aircraft at the time of acquisition has been reduced for depreciation purposes by an amount equal to the cost or estimated cost of the first overhaul. We have allowed amortization of the "built-in" overhaul under maintenance expenses, and have disallowed the accrual of depreciation on the value so eliminated, amounting to \$59,000 applicable to the equipment placed in operations during the review period.

In accordance with our findings as to excess equipment, we have made a disallowance of \$63,000 depreciation expense for the past period, applicable to the DC-3 cargo aircraft and related equipment.

In conjunction with the inauguration of service with the Convair 240 aircraft, Western retired five DC-3 aircraft during the period from September 1 to December 1, 1948. Depreciation on this equipment has therefore been eliminated in the amount of \$35,000.

Western had included in its accrual of depreciation, a total of \$178,000 applicable to estimated loss on retirement of DC-3 non-rotatable spare parts. After spreading depreciation to June 30, 1949, \$158,000 of this expense would have been accrued in the past period. We have stated in recent cases ¹⁵, however, that it is believed appropriate under 437 ordinary conditions to accrue such a reserve over a period at least two and a half years in advance of the estimated retirement date of the related aircraft. In this

¹⁵ *Braniff Airways, Inc. Mail Rates*, and *Delta Air Lines, Inc. Mail Rates*, *supra*.

instance the carrier plans to retire almost one half of its DC-3 fleet eight months prior to the common retirement date we have allowed herein, which should allow the carrier to reduce appreciably the inventory and, therefore, the loss on retirement. We will allow a reserve of \$100,000 to be accrued over the two and a half year period prior to June 30, 1949, a proportionate share of which has been allocated to Inland. Accordingly, the accrual allowable in the past period amounts to \$51,000, and we have eliminated \$107,000 charged in the past period. Of this amount, \$38,000 has been transferred to Inland, \$5,000 allowed in the future period and \$64,000 disallowed as applicable to equipment retired or disallowed from used and useful investment.

The total amount of the adjustment of DC-3 depreciation expense as a result of the foregoing is \$489,000.

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DC-4 Depreciation

The carrier established a four-year service life and a residual value of 10 percent for its DC-4 equipment. Since this policy is in accordance with the Board's allowance in the past for this type of equipment, we have accepted the computation of the carrier in this instance.

We have disallowed depreciation applicable to equipment which we have found in excess of reasonable requirements, amounting to \$176,728 for the past period. Of the total \$32,000 represents depreciation expense on excess R-2000 engines. The carrier claims, with some reason, we believe, that the total number of engines reported was necessary because of the abnormal failure rate experienced in the operation of Route 68. We regard this expense therefore as in the nature of a developmental expense. A contributing factor to the finding of excess engines was the sale of four DC-4 aircraft to United in 1947 in addition to three sold previously, two without engines. According to the carrier, the three DC-4's sold prior to the route sale were originally acquired for operation of the route. It is appropriate therefore to apply the engine depreciation removed from operat-

ing expense as an offset to the profit from sale of the route.

Although the Convair 240's will have replaced five DC-4's by December 31, 1948, or shortly thereafter, the carrier claimed depreciation expense on the DC-4's through March 31, 1949, since this equipment would be retained until that date as insurance against temporary withdrawal of the Convairs from service. We have maintained before ¹⁶ that such a contingency is one of the risks of doing business which is reflected as a normal cost of capital rather than as a
 439 normal cost of operations. It is not proper to allow the accrual of depreciation expense therefore on duplicate equipment, and we have disallowed \$62,000 applicable to DC-4 aircraft and engines replaced by Convair 240's in the past period.

The carrier estimated that it will experience a loss on the retirement of DC-4 non-rotatable spare parts of \$345,000, even though the DC-4's are being retired approximately a year and a half in advance of the retirement date originally estimated. These inventories were accumulated for a fleet of 13 DC-4's, which has been reduced to a fleet of five required for scheduled operations after disposing of Route 68. A proportionate amount of non-rotatable spare parts was not sold with the route or with the aircraft sold prior to the sale of the route. Accordingly we will allow the carrier to accrue a reserve amounting to approximately 25 percent of the depreciated cost less 10 percent residual value of non-rotatable spare parts at the date of the route sale, September 15, 1947, or \$200,000, and charge off this amount over the three year period prior to the actual retirement date of December 31, 1948. The carrier had accrued \$281,000 during the past period, of which \$81,000 will be disallowed for rate-making purposes. Since the loss estimated by the carrier over our allowance of \$200,000 is the result of the disposal of DC-4 equipment purchased for the operation of Route 68, it is

¹⁶ *Braniff Airways, Inc., Mail Rates, supra.*

proper that the disallowance of \$81,000 be treated as an offset to the profit from the sale of Route 68.¹⁷

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Convair 240 Direct Flying Costs

We have based our estimate of Convair 240 direct flying costs on results which it is expected the carrier will attain in the future year, and have discussed these in detail in our consideration of future year expenses. This estimate of \$126.63 per hour flown has been applied to the last four months of 1948. On the basis of 4,438 hours estimated for the last four months of 1948, we have allowed direct flying costs of \$562,000 for the Convairs.

Ground and Indirect Expenses

The carrier reported a total of \$22,167,000 of ground and indirect expenses for the entire past period. We have made adjustments to this total of \$1,123,000, leaving a balance of recognized expenses amounting to \$21,044,000, equal to 70.25 cents per revenue plane mile.

Reported expenses include amounts expended for charitable contributions and entertainment totaling \$52,000 for the years 1945 through 1947. We have consistently held in accordance with the general practice of rate-fixing bodies, that expenditures for charitable purposes as distinguished from payments to business and trade organizations should be eliminated from operating expenses in determining need for mail pay.¹⁸ With respect to entertainment expenses, the carrier has provided no basis for determining the necessity or reasonableness of such expenditures. As we have stated before in a recent case ¹⁹, "the very nature of enter-
441 tainment expenses is such as to make it virtually impossible to ascertain the extent of their need in an

¹⁷ The carrier had improperly accrued depreciation on non-rotatable spare parts rather than a reserve for loss on retirement. As a result, it had understated its accrual in relation to its estimated loss on retirement of \$345,000. Since only the amount of \$200,000 has been allowed herein, we have applied the balance of \$145,000 as an offset to the profit from the sale of Route 68, which amount includes the actual disallowance of \$81,000 of depreciation accrued.

¹⁸ *Delta Air Corp., Mail Rates*, 4 C. A. B. 501, 504 (1943).

¹⁹ *American Overseas Airlines, Inc., Mail Rates*, supra.

enterprise, and we are of the opinion that it is our duty under the Act to reject them for rate-making purposes." We have disallowed therefore the total of \$52,000 of expense in the past period.

In the twelve months ended September 30, 1947 Western realized the lowest ton-mile cost in its operating history. However, subsequent to the sale of Route 68 on September 15, 1947 the carrier's reported ton-mile cost rose sharply. The decreased scale of operations after the route sale is indicated by the 24 percent decline in available ton-miles in the calendar year 1948 from the previous year and the 32 percent decline in revenue ton-miles in 1948. Although the increase in unit cost may be attributable in part to the loss in economies related to size in general, a substantial part of the increased unit cost is believed to be related to the necessary lag involved in cutting back indirect cost to a proper level in relation to the reduced scale of operations. We believe that that portion of the increase in unit cost which is attributable to the lag in cutting back cost should be regarded as a cost of divestment of the route and accordingly, for rate making purposes, should be eliminated from operating expenses and charged against the profit realized from sale of the route. As set forth in Appendix No. 2 by individual control accounts, we have accordingly eliminated the amount of \$281,000 from reported operating expenses for the fourth quarter of 1947 and the amount of \$500,000 for the year 1948, and the total amount of \$781,000 of divestment cost has been charged against the profit realized from the sale of Route 68.

442 For the year 1946 we eliminated pre-operating and training expenses of \$48,000 applicable to DC-4 pilot training and inauguration of service on Route 68. We have allowed the carrier to capitalize this amount and to set up amortization over a five-year period from April 1, 1946, the date of inauguration of service. The unamortized balanced of \$34,400 as of September 15, 1946, has been charged to the profit from the route sale.

Prior to the sale of Route 68, Western had been allocating 15 percent of certain general and administrative expenses to Inland based on the ratio of volume of services performed by the two carriers. After the sale of the route, the ratio of cash operating expenses of Inland to the total increased to 23 percent. We have made an additional allocation therefore to Inland from October 1, 1947, amounting to \$18,000 and \$68,000 for 1947 and 1948, respectively. General and administrative expense has also been reduced by \$98,000 in 1947 and \$136,000 in 1948, which are part of the divestment costs applied against the profit from the route sale.

As we discussed previously with respect to incidental revenues, we have reduced operating expenses in 1948 by \$186,000, which represents the carrier's estimate of expenses incurred in producing the abnormally high incidental revenues. A large portion of expenses are station expenses incurred in the performance of services for others under joint agreements. We have accepted the carrier's estimates and have eliminated expenses from various accounts as follows: ground operations, \$100,000; traffic and sales, \$50,000; and general and administrative, \$36,000, such amounts being treated as a charge to net incidental revenues..

After making the foregoing adjustments, the total ground and indirect expenses on the basis of revenue ton-miles and available ton-miles for the years 1945-1948 become as follows:

| | Cents per Revenue Reported Expense | Ton-Mile Adjusted Expense | Cents per Available Reported Expense | Ton-Mile Adjusted Expense |
|------|--|---------------------------------|--|---------------------------------|
| 1945 | 30.13c | 29.92c | 24.67c | 24.50c |
| 1946 | 32.42 | 32.08 | 19.51 | 19.31 |
| 1947 | 34.50 | 32.70 | 18.74 | 17.77 |
| 1948 | 43.78 | 37.64 | 21.10 | 18.14 |

Although we have made adjustments in reported ground and indirect expenses of \$706,000 in 1948, expense per revenue ton mile is still considerably higher than in the preceding three years. Measured on an available ton mile basis, however, adjusted expense is approximately the average of 1946 and 1947, the period of operation of Route 68.

Pre-Operating and Training Costs

As we indicated in the above discussion, direct flying costs of \$126,000 for Route 68 pilot training and pre-operating costs of \$48,000, making a total of \$174,000, were eliminated from operating expenses and capitalized. We have allowed Western to amortize these expenses over a five-year period, which we have found to be reasonable for other carriers in the past ²⁰, and which would not burden any one year with non-recurring costs of this nature. Amortization of the total from April 1, 1946 to September 15, 1947, the date of the route sale, provides an additional \$51,000 of expense.

Western has been accumulating deferred charges relating to the acquisition of and inauguration of service with the Convair 240 aircraft. It estimates that total expense
 444 of this nature will amount to \$150,000, of which approximately \$100,000 is applicable to pilot training and familiarization flights. In view of the large scale substitution of Convairs for DC-3 and DC-4 aircraft, the necessity of having all pilots checked out on the new equipment for flexibility of scheduling crews, and the training of maintenance crews, as well as engineering and miscellaneous expenses related to purchase of the equipment, it appears that the carrier's estimate is reasonable. Accordingly, we have allowed the capitalization of \$150,000 as of September 1, 1948, the date service was inaugurated. Amortization on a five-year basis amounts to \$10,000 for the last four months of 1948.

Miscellaneous Credits

The carrier earned cash discounts income of approximately \$23,000 for the past period, which we have taken into account as a credit against operating expense in accordance with established Board policy.

²⁰ *Braniff Airways, Inc., Mail Rates, supra.*

Break-Even Need

In consideration of the foregoing, total operating expenses recognized for rate-making purposes amount to \$36,405,000 for the 56-month period. After deducting non-mail revenues of \$33,216,000, the net operating loss before mail pay is \$3,189,000. Western's need for mail pay, however, has been reduced by "other revenue" of \$116,000 from sale of operating property and of \$794,000 which we have found is the net gain to Western from the sale of Route 68. After giving effect to "other revenue" of \$910,000, break-even need before mail pay amounts to \$2,279,000, equal to 7.61 cents per revenue plane mile.

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Investment

The average investment on a reported basis and the adjustments we have made thereto for rate making purposes are shown in Appendix No. 5. Explanation of the major items of adjustments are included in the following discussion.

Working Capital

After the purchase of Inland in May 1944, the two companies were gradually integrated to the point where Western performed most of the purchasing functions for Inland and maintained most of the inventories used by the two companies. Because of the large number of inter-company transactions, it is appropriate to make an allocation of the combined working capital in accordance with the ratio of cash operating expenses. The average working capital has been computed in this manner for the years 1946-1948, and the results are shown in the attached appendix.

Western reported a negative working capital position from the quarter ended June 30, 1946, until September 30, 1947, due to the abnormal amount of notes payable included in current liabilities. These notes represented amounts due the Douglas Aircraft Corp. for conversion costs and deposits on new equipment, and borrowings from banks on a

short term basis for later conversion into long term debt. Because of the large losses incurred in the winter 1946-1947 as a result of the falling off of traffic demand and unfavorable flying conditions, and the resulting deterioration of its financial condition, the carrier was no longer able to finance its obligations through normal credit channels, and in consequence, made application for a loan from the Reconstruction Finance Corporation in the spring of 1947. This loan was approved and was received by Western in December 1947, in the amount of \$3,800,000, which together with the funds received from the sale of Route 68, enabled Western to redeem all of its short term notes outstanding. The amount of notes payable reached a total of more than \$5,000,000 at August 31, 1947, and accounts payable included approximately \$1,800,000 to the Austin Company for construction of the new hangar.

Recognizing that a major portion of the notes payable reported by Western as current liabilities was in substance long-term capital and was ultimately converted into long term debt, we have eliminated from current liabilities an average of \$1,652,000 in 1946 and \$2,833,000 in 1947 in making our computation of working capital.

447 In spite of this adjustment, however, average working capital for the year 1946 amounted to a minus \$67,000, and for the year 1947, to a minus \$816,000. After giving effect to the pro-rate with Inland and adding in retroactive mail pay beginning at the first of the year 1946, average working capital becomes a plus \$139,000 for 1946, and a minus \$469,000 for 1947.

Western also reported negative working capital in the last six months of 1948 because of payments on its RFC loan which were due within one year. However, in computing working capital, we have eliminated from current liabilities an average of \$227,000 of notes payable which became current in this period. These notes are considered applicable to DC-4 equipment which has been replaced by Convairs and accordingly eliminated from the rate base. Since

this equipment is shortly to be sold, the carrier has on hand assets which are to be converted into cash or its equivalent. We have discussed in greater detail in the future period the treatment of negative working capital under such circumstances. After reflecting retroactive mail pay of \$567,000 after taxes, and allocation of working capital to Inland of \$90,000, average working capital for 1948 becomes \$446,000. This and other computations of working capital have been set forth in Appendix No. 5.

Investments and Special Funds

Western's investment in Inland has been eliminated from the rate base, since mail rates are fixed separately for that carrier, and including this investment for Western would result in duplicating the rate of return provided on Inland's investment.

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Equipment Purchase Funds

In a previous opinion²¹ we have allowed the capitalization of interest expense on equipment purchase funds prudently and properly set aside for major expansion programs requiring substantial capital outlays. In the instant case, Western made deposits on Convair aircraft and Pratt & Whitney engines in the first quarter of 1946. In 1947 and 1948, Western also reported Convair spare parts and engines in its flight equipment investment, which we have eliminated as indicated previously. The amounts of deposits and investment in equipment for the period up to September 1, 1948, when Convairs were placed in revenue service, averaged \$600,000. Because of a shortage of working capital during the period when funds were initially advanced and up to inauguration of operations, Western found it necessary to secure additional capital through short and long term loans. At no time during the time that deposits were outstanding was the indebtedness less than the deposits. In determining the amount of interest which

²¹ *Braniff Airways, Inc., Mail Rates, supra, Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C.A.B. 267 (June 9, 1947).

should be capitalized, we have therefore used the rate paid by Western, amounting to 3 percent to December 1947, and 4 percent to September 1948, rather than a rate of 5 percent which would be appropriate in the event there was no outstanding debt. The interest so computed amounts to \$52,069, which we will add to the investment in Convair equipment and allow Western to amortize over the seven-year estimated service life from September 1, 1948. Although the period over which deposit funds were outstanding appears long, the low price at which the carrier was able to acquire the equipment compared to the subsequent
 449 price increases justifies considering the full amount of funds invested over the entire period.

Operating Property and Equipment

The carrier owned certain miscellaneous types of aircraft, which it either rented to Inland or operated in non-revenue service. The Lodestar and Stinson, which were rented to Inland in 1944 and 1945, have been eliminated from investment, but the direct flying costs disallowed from operating expenses have been offset from non-mail revenues as we indicated above. Three AT-6 aircraft were acquired by Western in 1946, primarily for training. Very little training was accomplished with these aircraft, and they were sold to Inland in 1947. They have accordingly been removed from Western's recognized investment as not used and useful investment.

The carrier included one DC-3 aircraft in its investment at December 31, 1944, which was not placed in scheduled service until 1945. The net book value of \$37,739 has been eliminated from investment on that date.

The carrier had construction work in progress of approximately \$200,000 at the end of 1945, representing conversion costs on DC-3 aircraft. Since these aircraft were not placed in service until 1946, this amount has been eliminated from the investment at December 31, 1945.

In accordance with our previous finding as to excess equipment, we have eliminated from investment DC-3 cargo

aircraft No. NC-56589 from January 1946 until July 1947, when it was converted into a passenger aircraft. The DC-4 cargo aircraft has been eliminated from investment 450 for the entire past period.

As we have indicated in the section on equipment purchase funds, all investment in Convair equipment has been eliminated from allowable flight equipment until September 1, 1948. As of December 31, 1947, spare parts totaled \$76,000 and spare engines, \$143,000. These amounts increased to \$202,000 and \$325,000, respectively, as of September 1, 1948.

In the summer of 1947, Western moved into its new hangar and office building at the Los Angeles Municipal Airport. The cost of the hangar was about \$2,500,000, which the carrier has been depreciating from July 1, 1947, on the basis of a 30-year life. We have established herein a basis of allocation of general and administrative expenses between Western and Inland of 77 and 23 percent, respectively, from October 1, 1947, based on the ratio of cash operating expenses of the two companies. It is appropriate, therefore, to allocate the investment in the hangar on the same basis. We have reduced Western's investment in the hangar, therefore, by 23 percent, or \$575,000 of the original cost as of July 1, 1947, and transferred this amount to Inland.

Other Investment Items

Pre-operating and training expenses capitalized in the amount of \$174,000 at April 1, 1946, show a balance at December 31, 1946, of \$148,000 and at the time of the route sale, the unamortized balance is \$123,000, which was removed from investment and offset against the reported profit from the sale. Convair 240 pre-operating expense is included in the rate base from September 1, 1948, and the unamortized balance at December 31, 1948, is \$140,000.

We have recognized extension and development expense of \$80,717 covering the entire past period, representing

reasonable and necessary expenses incurred in route
451 cases in which the carrier received an award. This
expense as it pertained to a particular route or station was capitalized as of the time service was inaugurated, and amortized over a five-year period. We have disallowed the total of \$43,000 of expense incidental to the award of the route from Los Angeles to Mexico City and to the extension of Route 52 from Lethbridge to Edmonton, Canada, until such time as service is inaugurated on these routes.

Determination of Mail Pay

We have indicated previously that the break-even need before mail pay for the past period amounted to \$2,279,000. In addition to this amount, the carrier is entitled to a fair return on the recognized investment. Because of the fact that for a past period the probability of error in estimating results has been removed, and except for the fourth quarter of 1948, these results are now known, it is customary to provide a lower rate of return than for a future period. We have allowed, therefore, a return of seven percent per annum on the recognized investment after allowance for Federal income taxes.

Seven percent on the average investment for the past period from May 1, 1944 through December 31, 1948, after provision for Federal income taxes, amounts to \$1,973,000. In computing income taxes we have applied interest expense amounting to \$391,000 for the period as a deduction from the return allowed herein in order to determine the net taxable income. We find, therefore, that the fair and reasonable compensation for the transportation of mail by aircraft for the entire past period from and including May 1, 1944 through December 31, 1948 is \$4,252,000, equal to 14.20 cents per revenue plane mile flown in scheduled service. This amount is inclusive of and not in addition to mail compensation already received from May 1, 1944, up to and including December 31, 1948.

452 MAIL RATE FOR THE PERIOD ON AND AFTER
JANUARY 1, 1949

The period for the determination of a future rate is selected to run from January 1, 1949, since this date represents the beginning of operations with the complete Convair 240 fleet. Inasmuch as this type of aircraft will account for approximately 80 percent of the revenue mileage to be operated in the future year, and since the overall cost pattern and investment pattern will be substantially changed after the full fleet is in operation, it is proper that operations be reviewed on the basis of the new equipment.

Scheduled Services Required

The estimate of revenue miles to be operated in the future period is 6,202,727 or 2 percent below that operated in 1948. This mileage will produce, however, 12.3 percent additional seat miles and 15.4 percent additional passenger miles at a 57 percent passenger load factor. This increase is made possible by the substitution of the Convair 240 for five DC-3 and five DC-4 aircraft on a large portion of the route segments, thereby increasing the average number of seats available per mile from 31 in 1948 to 36 in 1949.

In spite of the increase in seat miles, it is estimated that the passenger load factor will increase from 55 percent in 1948 to 57 percent in the future year. In view of the high average seats per mile flown estimated in the future year, which exceed the average of all other carriers in the intermediate group except National, we find that a 57 percent load factor is reasonable for this carrier.

The schedule pattern will remain approximately the same in 1949 as in 1948, as indicated in the following table. One additional round trip will be scheduled over the coastal route in the second and third quarters, and one less round trip will be scheduled over Route 13 from Los Angeles
453 to Salt Lake City as a Result of the substitution of one Convair trip for two DC-3 trips.

| Segment | Average Round-Trip Frequency | | Passenger Load Factor | |
|----------------------------|------------------------------|------|-----------------------|-------|
| | 1948 | 1949 | 1948 | 1949 |
| Los Angeles-San Francisco | 7.8 | 8.5 | 60.5% | 60.7% |
| San Francisco-Seattle | 3.0 | 3.5 | 43.7 | 50.9 |
| Los Angeles-San Diego | 4.0 | 4.0 | 60.4 | 56.3 |
| San Diego-Yuma | 0.5* | 0.5* | 38.3 | 42.5 |
| Los Angeles-Salt Lake City | 3.3 | 2.5 | 65.4 | 61.2 |
| Salt Lake City-Great Falls | 2.0 | 2.0 | 58.2 | 57.6 |
| Great Falls-Lethbridge | 1.0 | 1.0 | 45.5 | 46.8 |
| Total | 3.2 | 3.2 | 55.1% | 57.0% |

*Three days a week only.

It will be noted from the above table that in 1948 the segments with the highest frequencies had the best load factors, with the exception of the San Francisco-Seattle segment, which was placed in operation in August 1947, and had not reached full development in 1948. The carrier estimated that it would operate additional frequencies on the coastal route over those we have provided for herein. In this event, however, it is presumed that the additional revenues so derived will more than offset expenses incurred, and the return to the carrier will be increased thereby.

In view of the foregoing, we find that all of the scheduled services estimated herein are necessary in the interests of one or more objectives of the Act.

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Equipment

By January 31, 1949, according to recent plans, Western will have placed in service all ten of the Convair 240's which are on order, replacing five DC-3 and five DC-4 aircraft. The change of equipment will effect economies in over-all aircraft operating costs, which will be reduced from the 61 cents per mile experienced in 1948 to approximately 59 cents per mile in 1949. Due to the increase in average seats per plane, the effect on the cost per seat-mile is more significant, decreasing from an average of 1.90 cents in 1948 to 1.64 cents in 1949.

Daily revenue utilization of the combined fleet of Convairs and DC-3's is estimated at 6:45 in the future year, compared to 7:51 per operating aircraft in 1948. Although

it is reasonable to expect lower utilization of new equipment during the initial period of operation while operations and maintenance personnel are becoming familiar with the aircraft, a more significant factor relating to the lower utilization is the increase in speed of the Convair over the DC-3 and DC-4 aircraft replaced, without a corresponding increase in miles operated. In fact, estimated revenue plane miles are 2 percent less than operated in 1948. In view of the 7:36 utilization which Western expects to attain in the peak summer operations, we find that 10 Convair 240's and four DC-3's will be required for scheduled operations.

Estimated Operating Results

The revenues, expenses, and break-even need estimated by Western for the future period are set forth in Appendix No. 3, together with adjustments deemed appropriate for rate making purposes. The principal adjustments are explained below.

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Non-Mail Revenues

Total non-mail revenues are estimated at \$8,134,000 for the future year, or an increase of 22 percent over the \$6,670,000 expected to be realized in 1948. The higher revenues are mostly due to the 15 percent increase in passenger miles at a 57 percent load factor which coupled with the increase in passenger fares, averaging 8 percent with a 5 percent round-trip discount, instituted September 1, 1948, are expected to produce 23 percent greater passenger revenue than in 1948.

Cargo revenues are estimated to increase slightly in the future year. The carrier estimates freight revenues at \$179,000 compared to \$158,000 expected in 1948, and express revenues show a decrease from \$98,000 to \$88,000. Since Western's estimates are in line with recent trends experienced by it, we shall accept the carrier's estimates of express and freight revenues.

Charter and incidental revenues were estimated by the carrier at \$194,000, compared to \$286,000 expected to be

realized from this source in 1948. This estimate does not include potential revenues from rental of excess office and shop space in the new hangar building, and from performance of maintenance for other operators by reason of maintenance facilities which are in excess of normal requirements. The carrier estimates that approximately 456 \$66,000 may be realized from these sources, which amount, when added to the original estimate, increases the total to \$260,000 for the future year. In producing the total incidental revenues, the carrier claims that it will incur expenses of \$150,000. Therefore, it is proper, in order to avoid distortion of operating expenses required for normal operations, to reduce expenses by this amount and to offset an equal amount from incidental revenues. Net incidental revenues included for rate making purposes thus become \$110,000.

We have taken into account therefore in fixing the future mail rate total non-mail revenues of \$8,134,000 equal to 131.1 cents per revenue plane mile at a 57 percent passenger load factor.

Operating Expenses

Operating expenses allowed herein for the future year are set forth in Appendix No. 3, together with the adjustments deemed necessary for rate making purposes. An explanation of the more important adjustments is included in the discussion which follows.

DC-3 Direct Flying Costs

We have estimated DC-3 direct flying costs on the basis of the experience for the first six months of 1948, after a correction for the economies expected to be realized by the carrier in the operation of its own engine overhaul shop scheduled to go into effect shortly after the beginning of the period. The carrier estimates that it will be able to reduce engine overhaul costs by 25 percent, which will lower total direct maintenance costs from \$16.99 to \$15.82 per hour.

Convair 240 Direct Flying Costs

We have estimated direct flying costs for the Convair 240 at \$126.63 per flight hour, or 60.6 cents per mile at an average airport-to-airport speed of 209 miles per hour, expected to be realized on an average trip length of 250 miles over Western's routes. The breakdown of the component costs is as follows:

| | Per Hour | Per Mile |
|--------------------|----------|----------|
| Flying Operations | \$ 62.92 | 30.11c |
| Direct Maintenance | 49.90 | 23.88 |
| Depreciation | 13.81 | 6.61 |
| | <hr/> | <hr/> |
| Total | \$126.63 | 60.60c |

In estimating direct maintenance expenses, we have given effect to the estimated economies which the carrier expects to realize from operation of its own engine overhaul shop shortly after the beginning of the future year. The carrier expects to arrange for overhaul of pressurization equipment outside its own shop, and it is not practical to make special provision for this particular item in our estimates. In view of the limited cost experience available on this type of equipment, we have used costs of other equipment types as well as the initial reported Convair maintenance cost of American Airlines as a basis for arriving at an estimate of maintenance expense which the carrier should be able to realize through efficient operations. Also because of certain features in the design of the aircraft which provide ready access to components for inspection and routine maintenance, it may be possible for the carrier to realize costs lower than those provided herein, and thereby increase the earning power of the equipment.

We have established a service life of seven years for the Convair 240 aircraft and engines and residual values of \$25,000 for the hulls and \$500 for engines. The carrier has estimated the value of the "built-in" overhaul at \$30,000 for the hulls and \$4,067 for each engine. These amounts

have been deducted from the original cost, and allowance provided in maintenance expense for the amortization of these values over the first overhaul period.

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Ground and Indirect Expenses

Western estimated ground and indirect expenses at \$5,429,000 for the future year, compared to \$5,162,000 for the year 1948. Most of this increase is accounted for by general and administrative and passenger service expense. The increase in the latter is considered reasonable in view of the estimated 15 percent increase in passenger miles forecast for the future year over 1948. The estimate of general and administrative expense of \$1,070,000, however, is 19.4 percent higher than reported in 1948, and is equal to 13.4 percent of other cash operating expenses, which is unreasonably high in relation to such expense allowed by the Board in recent cases for carriers of approximately the same size.²²

The carriers estimate of general and administrative expense reflected an allocation to Inland of 15 percent of allocable expense. We have found in our discussion of the past period that a 23 percent allocation more nearly represents the proper ratio of allocation. Accordingly, we have eliminated \$84,000 from Western's estimate as additional expense to be borne by Inland.

As we indicated in our discussion of non-mail revenues, it is appropriate to reduce operating expenses for the future year by the abnormal expense of producing the large incidental revenues estimated by the carrier in order to adjust expenses to a level which may be compared to other carriers. Of the total adjustment of \$150,000, it is estimated that \$5,000 is applicable to general and administrative expense. The balance of \$145,000 has been eliminated from ground operations, ground and indirect maintenance, and traffic and sales expenses.

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²² *Chicago & Southern Air Lines, Inc., Mail Rates*, Docket Nos. 1335 and 1897 Order Serial No. E-1825 (July 28, 1948); *Delta Air Lines, Inc. Mail Rates*, *supra*.

We have made a further adjustment to general and administrative expense estimated in the future year of \$146,000, which is considered in excess of a reasonable level of expense for the estimated volume of operations. This adjustment is reduced, however, by allowance for wage and price increases, including pay roll taxes and insurance. The total adjustment of the carrier's estimate of general and administrative expense for the future year is therefore \$200,000, reducing allowable expense from \$1,070,000 to \$870,000, approximately 11.7 percent of all other cash operating expense. In making this allowance we have taken into consideration the high level of personal property taxes which the carrier pays on property located in Los Angeles County. In 1947, this tax amounted to approximately \$160,000, or 1.03 cents per available ton-mile. The industry average for this item is 0.55 cents per available ton-mile. On the basis of the available ton-miles forecast for 1949 and assuming that the differential from the industry average will remain the same, Western would have a tax liability approximately \$120,000 greater than if it paid a tax at the same rate as the industry.

Total ground and indirect expense allowed for rate making purpose is therefore \$5,207,000, equal to 83.94 cents per revenue plane mile.

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Wage and Price Increases

The carrier claims that it will experience increased salary and wage costs in the future year of \$288,000, partly because of negotiations which have been under way for several months and which will result in increases effective in 1948. It also claims that estimates for the future year have been based on 1948 experience without adjustment for anticipated price increases of \$184,000. There is no sound basis, however, to indicate that a large part of the wage and price increases anticipated by Western will in fact materialize. On the other hand, some wage increases and higher prices for gasoline and lubricants and aircraft parts have

already occurred and are not fully reflected in the estimates for the future year. Also Western increased passenger fares to yield approximately 8 percent higher revenues in the future which places part of the burden of cost increases on non-mail services, as we have indicated as proper in a recent case.²³ We will make an allowance therefore for wage and price increases in the future year which are known or appear to be imminent amounting to \$215,000, equal to approximately three percent of adjusted cash operating expenses.

Total Operating Expenses

As mentioned previously in our discussion of the past period, we have allowed the carrier to capitalize \$150,000 of training and pre-operating costs in connection with the inauguration of service with the Convair 240. Amortization has been set up over a five-year period, in accordance with which we will allow \$30,000 amortization in the future year.

Amortization of extension and development expense capitalized previously amounts to \$6,000 for the future
461 year.

We have estimated cash discount income at \$5,000 based on the carrier's experience in 1948, and have credited this amount to operating expenses.

As a result of the foregoing adjustments, therefore, total operating expenses allowed for rate making purposes in the future year amount to \$8,911,000, equal to 143.66 cents per revenue plane mile.

Break-Even Need

The adjusted break-even need before mail pay based on non-mail revenues of \$8,134,000 and operating expenses of \$8,911,000 is \$777,000, equal to 12.52 cents per revenue plane mile estimated to be flown in scheduled services.

Investment

The rate base for the future period is based on the proforma balance sheet as of December 31, 1948, and reflects

²³ Chicago and Southern Air Lines, Inc., Mail Rates, *supra*.

the substitution of the Convair 240 aircraft for the DC-3 and DC-4 aircraft replaced. We have recognized an investment of \$7,064,000 for rate making purposes, which is summarized with explanations of adjustments in Appendix No. 6.

Working Capital

We have estimated the carrier's net working capital at December 31, 1948, at a minus \$1,619,000, based on reported working capital at September 30, 1948, and estimated results for the fourth quarter of 1948. This amount also reflects an allocation of \$31,000 of working capital to Inland based on the ratio of estimated cash operating expenses of the two carriers in the future year. After taking into account retro-active mail pay of \$680,000,²⁴ negative working capital is reduced to \$939,000.

The carrier's negative working capital position is the result of including in current liabilities \$1,824,000 of payments due within one year on the total RFC loan of \$6,100,000. Of the total, \$1,200,000 represents payments on the first loan of \$3,800,000, and \$624,000, payments on the second loan of \$2,300,000, covering purchase of the Convair 240's.

If the computation of working capital in this instance were restricted to the common definition of current assets minus current liabilities, then we would be overlooking the sum and substance of the factors included in the computation. Here we have a situation in which debt incurred for the purchase of physical operating property has reached a maturity of less than one year. A large portion of this debt was necessary to buy equipment in advance of the time that

²⁴ This amount was computed for the period May 1, 1944 to December 31, 1948, as follows:

| | |
|--|-------------|
| Mail compensation established herein | \$4,252,000 |
| Estimated Mail pay accrued for the period | 3,277,000 |
| Additional mail pay provided | \$ 975,000 |
| Estimated Federal income taxes | 295,000 |
| Additional mail pay added to working capital | \$ 680,000 |

the replaced equipment would be sold. The carrier is already taking action to dispose of the DC-3 and DC-4 equipment replaced by the Convairs, the book value of which in the amount of \$1,469,000 we have eliminated from the rate base. If we were also to include in current liabilities that portion of the debt applicable to both the old and new equipment, then we would be failing to give recognition to working capital that the carrier now possesses and requires for current operations. Another source of funds which the carrier will have available during the year is the return on investment of approximately \$563,000 we have provided herein for the future year. This amount together with the proceeds from sale of equipment will more than offset the notes payable of \$1,824,000. We find it therefore appropriate under the circumstances peculiar to this case to eliminate all notes
 463 payable from current liabilities in computing working capital for rate-making purposes. Net working capital of the carrier thus becomes \$885,000, the equivalent of slightly more than one month's cash operating expenses.

Operating Property and Equipment

The carrier's estimated investment in operating property for the future year of \$8,137,000 included DC-3 and DC-4 flight equipment being retired from scheduled service, and which it wished to retain as insurance against possible temporary difficulties with the Convair 240. Since this equipment is in excess of operating requirements, we have eliminated \$1,469,000 from the investment at December 31, 1948. The retention of this equipment as insurance against the grounding of its new aircraft is the prerogative of prudent management, but the added capital costs should be recognized only through the allowable rate of return rather than through an overstatement of the investment.

In accordance with the policy adopted for the past period, we have allocated a proportionate share of the investment in the new hangar to Inland in the amount of \$546,000, equal to 23 percent of the depreciated cost as of December 31,

1948. We have also allocated 3.25 DC-3 aircraft to Inland plus a pro-rata share of spare engines and other spare parts and assemblies equivalent to \$106,000, making a transfer to Inland of a total amount of \$652,000. We have recognized operating property and equipment therefore of \$6,016,000 for the carrier for the future year.

Other Investment Items

The investment in Inland Air Lines, has been eliminated as in the past period, since we have fixed separated 464 mail rates for this subsidiary. Western's investment was reduced accordingly by \$396,000, the book value estimated by the carrier at December 31, 1948.

Other items included in the rate base are \$140,000 of unamortized preoperating and training costs applicable to the inauguration of service with the Convair 240's, and \$15,000 of unamortized extension and development expense.

After making the foregoing adjustments, we find that the carrier's investment for rate making purposes amounts to \$7,064,000 for the future year.

MAIL RATES

Base Mileage

The rate established herein will contain an automatic adjustment formula which will serve to reduce the prescribed base mail rates to lower effective rates in inverse proportion to any increases in scheduled mileage over the prescribed base mileage.

The base mileage as well as the other factors involved in the automatic adjustment formula is stated in terms of airport-to-airport distances on an all-stop basis, computed via all certificated intermediate points between trip terminals. An exception has been made, however, for the computation of mileage on Route 13 between the terminal point San Diego and the intermediate stop Los Angeles so as to reflect scheduled miles as flown rather than all-stop miles. Computation of mileage on the basis of the present certificate re-

sults in an overstatement of approximately 2,000 miles daily in relation to mileage as scheduled by the carrier, and would unnecessarily distort the base mail rate. Another factor we have considered is the carrier's petition before the Board for the transfer of a portion of Route 13 to Arizona

465 Airways, which if granted, would result in an effective mail rate under the proposed formula which would be higher than that we have found to be reasonable in the future year. Accordingly, the all-stop mileage of 18,584 estimated to be flown in the period of lowest schedule frequencies becomes 16,561 after giving effect to the revised computation with respect to Route 13 mileage.

In accordance with Board policy as set forth in recent decisions, we will establish a base mileage of 16,300 which is slightly less than the revised all-stop mileage of 16,561 to be flown in the period of the lowest forecast schedule frequencies. To offset the low base mileage, the base mail rates will be increased proportionately, so that the effective mail rate per revenue plane mile flown, after operation of the automatic adjustment formula, will constitute fair and reasonable mail compensation in accordance with our determination of the carrier's need. The combined effect of the higher base rate and lower base mileage will be to distribute mail payments more nearly equally by months, and at the same time provide a safeguard against over-scheduling in off-peak seasons with a view to maximizing the mail compensation payable under the formula.

Determination of Sliding Scale Mail Rate

In conformance with the mail rate formula developed in recent cases,²⁵ we will establish for the period on and after January 1, 1949, a sliding scale incentive mail rate formula, which will be reasonable in terms of an attainable passenger load factor and will decline with increases in the pas-
466 senger load factor at a rate designed to allow a progressive increase in the profit earned by Western.

²⁵ *Braniff Airways, Inc., Mail Rates, Chicago and Southern Air Lines, Mail Rates, and Delta Air Lines, Inc., Mail Rates, supra.*

Under the formula a maximum base mail rate of 33.00 cents per revenue plane mile will be earned by Western in each month when the passenger load factor is below 55 percent, computed on the basis of 21 passenger seats per DC-3 aircraft, 40 seats per Convair 240 aircraft, and 50 seats per DC-4 aircraft. For each one percent increase in the passenger load factor above 54 percent, the base mail rate will be decreased by 1.40 cents per revenue plane mile. The minimum base mail rate of 8.40 cents per revenue plane mile will be applicable when the passenger load factor is 72 percent or higher. As we have pointed out previously, however, in no month so long as the anticipated service pattern is operated, will the carrier receive an effective rate as high as the base rate, since the base mileage has been set below the lowest forecast frequencies for the lowest seasonal point of the year. The full scale of intermediate variations is presented in Appendix No. 7.

In the table below is shown the relationship between the base and effective mail rates and the rate of return at various passenger load factors. The sliding scale formula will enable Western to break even at a slightly more than 49 percent load factor and provides increase in the rate of return with each increment in the load factor.

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Sliding Scale Mail Rate

| Revenue Passenger Load Factor | Sliding Scale Mail Rates per Mile | Operating Income Before Income Taxes Per Revenue Plane Mile | % Return on Recognized Investment After Income Taxes |
|-------------------------------|-----------------------------------|---|--|
| | Base Rate | Estimated Effective Rate | |
| 50% | 33.00c | 29.52c | 1.4% |
| 55 | 31.60 | 28.27 | 7.0 |
| 57 | 28.80 | 25.76 | 8.0 |
| 60 | 24.60 | 22.01 | 9.5 |
| 65 | 17.60 | 15.75 | 12.1 |
| 70 | 10.60 | 9.49 | 14.7 |

The average mail load carried by Western in the first nine months of 1948 was equal to 155.0 pounds per revenue plane mile flown. Although the mail loads for any one month may exceed this average, the passenger load factors and cargo

loads for the foreseeable future leave ample capacity to accommodate the maximum probable mail loads in the future period, even after allowing for a substantial increase in mail volume as a result of air parcel post service which was inaugurated on September 1, 1948. Accordingly, the sliding scale mail rate prescribed herein will be without reference to base poundage of mail.

Conclusion

On the basis of the foregoing considerations, we find that the fair and reasonable rates of compensation to be paid Western for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its routes within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada, are as follows:

468 (a) For the period beginning May 1, 1944, and ending December 31, 1948, the amount of \$4,252,000.²⁶

(b) On and after January 1, 1949, for each month during which the average passenger load factor (computed in the manner set forth below) does not exceed 54.99 percent, a base rate of 33.00 cents per airplane mile; for each month during which the average passenger load factor exceeds 54.99 percent, a base rate per airplane mile which shall be less than 33.00 cents by 1.40 cents per airplane mile for each one percent, or fraction thereof, by which the average passenger load factor exceeds 54.99 percent, provided that in no event shall the base rate per airplane mile be less than 8.40 cents; said average passenger load factor per month shall be computed to the nearest hundredth of one percent and shall be derived by dividing the total revenue passenger miles flown in scheduled passenger service during the month by the total seat miles operated during the month, the total

²⁶ This amount of mail pay is equal to 14.20 cents per revenue plane mile flown in scheduled service.

seat miles to be derived by multiplying the number of miles operated in scheduled passenger service with each type of aircraft by the following standard number of seats established for purposes of this computation for such aircraft:

DC-3 type aircraft—21 seats;

Convair 240 type aircraft—40 seats;

All four-engine aircraft types—50 seats.

said base rates, which are set forth in Appendix No. 7 hereof for each average passenger load factor, and the effective rates per airplane mile to be derived therefrom shall be paid on the mileage (without regard to any base poundage of mail) and under the terms herein stated, as follows:

(1) For each month during which the average daily scheduled mileage is not greater than the average daily designated mileage and does not exceed 16,300 miles, the appropriate base rate per airplane mile set forth in Appendix No. 7.

(2) For each month during which the average daily scheduled mileage exceeds the average daily designated mileage but does not exceed 16,300 miles, an effective rate per airplane mile (computed to the nearest hundredth of a cent) which bears the same relation to the appropriate base rate per airplane mile set forth in Appendix No. 7 as the average daily scheduled mileage bears to the average daily designated mileage.

(3) For each month during which the average daily scheduled mileage exceeds 16,300 miles, an effective rate per airplane mile (computed to the nearest hundredth of a cent) which bears the same relation to the appropriate base rate per airplane mile set forth in Appendix No. 7 as 16,300 miles bears to the average daily designated mileage.

The aforesaid rates per airplane mile shall be applied to the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster

General for the carriage of mail; provided, however, that if any scheduled flight is operated in two or more sections between any two points served for mail and mail is transported on more than one such section, the aggregate of the sections so used shall, for all purposes of computing compensation except the computation of the average passenger load factor, be treated as a single flight, and the rates shall be applied to the airport-to-airport mileage flown by that section which covers the greatest airport-to-airport mileage between points served for mail.

The average daily scheduled mileage shall consist of the mileage of all scheduled trips, exclusive of trips cancelled by management with a view to reducing the volume of service operated, and the average daily designated mileage shall consist of the mileages of all scheduled trips designated or ordered to be established by the Postmaster General for the carriage of mail; such mileages shall be computed as though the mileage of each trip were the airport-to-airport distance via all certificated points along the flight route between the terminals of each trip, with the exception that, on trips serving the points in the certificate of public convenience and necessity between the terminal point San Diego and the intermediate point Los Angeles on Route 13, the scheduled mileage and designated mileage of trips scheduled (1) between San Diego and Yuma, (2) between San Diego and Los Angeles, and (3) between Los Angeles and Palm Springs, shall be computed as though such mileage were the distance via the certificated stop points between the above named points in the sequence set forth for each trip in the carrier's schedules filed with the Board. The average daily scheduled mileage and the average daily designated mileage shall be determined for each calendar month by taking the average (computed to the nearest mile) of the daily mileages of regularly scheduled trips, exclusive of trips cancelled by management with a view to reducing the volume of service operated, and of regularly designated trips, respectively, for the seven days

of the week, without regard to any variations of scheduled or designated mileages, respectively, on holidays.

The compensation provided herein shall be inclusive of and not in addition to the mail compensation heretofore received by the carrier for mail transported on and after May 1, 1944.

An appropriate order will be entered.

Traffic Statistics

For the Past Period and as Estimated for a Future Year

| | 8 Months Ended | 12-31-44 | 12-31-45 | 12-31-46 | 12-31-47 | 12-31-48 | Future Year Western Estimate | As Adjusted |
|--|----------------------|----------------------|----------|----------|--------------------|----------|------------------------------------|----------------|
| Revenue Plane Miles (000) ¹ | 2,302 | 5,286 | 8,614 | 7,388 | 6,361 | 6,326 | 6,203 ² | |
| Revenue Passenger Miles (000) ² | 42,486 | 94,357 | 191,660 | 166,396 | 108,560 | 127,357 | 127,290 | |
| Available Seat Miles (000) ² | 46,493 | 108,390 | 265,677 | 268,446 | 196,966 | 228,454 | 223,316 | |
| Passenger Load Factor ² | 91.38% | 87.05% | 72.14% | 61.98% | 55.12% | 55.75% | 57.00% | |
| Revenue Ton-Miles (000) ² | | | | | | | | |
| Passenger ³ | 4,036 | 8,964 | 18,208 | 15,808 | 10,313 | 12,098 | 12,093 | |
| Express | (131) ⁸ | (280) ⁵ | 422 | 399 | 285 | 292 | 251 | |
| Freight | (—) ⁸ | (—) ⁵ | 188 | 441 | 647 | 994 | 852 | |
| Excess Baggage | 55 | 85 | 137 | 133 | 90 | 137 | 109 | |
| Mail | 701 | 1,054 | 652 | 637 | 455 | 540 | 540 | |
| Total | 4,923 | 10,387 | 19,607 | 17,418 | 11,790 | 14,061 | 13,845 | |
| Available Ton-Miles (000) ⁴ | 5,525 | 12,686 | 32,585 | 32,064 | 24,463 | 25,459 | 25,172 | |
| Payload Factor | 89.10% | 81.9% | 60.2% | 54.3% | 48.20% | 55.23% | 55.00% | |
| Average Route Miles Operated | 1,685 | 1,701 | 2,401 | 2,726 | 2,698 | 2,698 | 2,698 | |
| Average Daily Round Trip Frequency | 2.79 | 4.19 | 5.03 | 3.76 | 3.22 | 3.21 | 3.17 | |
| Revenue Ton-Miles per Route Mile per Day | 11.93 | 16.73 | 22.37 | 17.51 | 11.94 | 14.28 | 14.06 | |
| Average Passenger Journey | 437.5 | 405.3 | 399.6 | 403.9 | 399.6 | — | — | |
| Average Daily Revenue Hours Flown per Revenue Aircraft | 8:31 | 9:31 | 7:45 | 7:21 | 7:51 | 6:00 | 6:45 | |
| Revenue per Ton-Mile (cents) | | | | | | | | |
| Passenger | 55.22 | 53.30 | 51.40 | 54.63 | 60.71 | 63.56 | 63.57 | |
| Express | (50.55) ⁵ | (48.17) ⁵ | 41.07 | 36.23 | 34.39 | 30.14 | 35.00 | |
| Freight | (—) ⁵ | (47.86) ⁵ | 30.12 | 27.18 | 24.42 | 18.00 | 21.00 | |
| Excess Baggage | 56.00 | 51.92 | 49.46 | 52.88 | 58.89 | 55.47 | 63.30 | |
| Mail | 59.97 | 60.35 | 112.34 | 153.36 | 114.07 | — | — | |
| Revenue per Passenger Mile (cents) | 5.25 | 6.06 | 4.88 | 5.19 | 5.77 | 6.04 | 6.04 | |
| Average Mail Load (pounds) | 609.0 | 398.6 | 154.6 | 182.2 | 155.0 ⁶ | — | — | |

APPENDIX No. 1

*Explanatory Notes**Explanatory Notes*

¹ Scheduled and non-scheduled service.

² Scheduled service only.

³ Computed on the basis of 190 lbs. per passenger including free baggage.

⁴ Computed on the basis of standard weights as follows:

DC-3 — 2.4 tons

DC-4 — 6 tons

CV-240 — 4.5 tons

Lodestar — 1.5 tons

⁵ No segregation of freight data reported prior to July 1, 1945.

⁶ Estimated from actual data for first nine months.

• • • • •

| Year 1948 | | 56 Month Period | | | Per Revenue Plane Mile As Adjusted |
|----------------|----------------|-----------------|-------------|----------------|--|
| As Reported | As Adjusted | As Reported | Adjustments | As Adjusted | |
| \$ 6,261 | \$ 6,261 | \$31,262 | \$ - | \$31,262 | 104.38¢ |
| 98 | 98 | 618 | - | 618 | 2.06 |
| 158 | 158 | 337 | - | 337 | 1.13 |
| 53 | 53 | 266 | - | 266 | .89 |
| 286 | 100 | 1,077 | -344 A | 733 | 2.45 |
| \$ 6,856 | \$ 6,670 | \$33,560 | \$ -344 | \$33,216 | 110.90¢ |
| | | | | | |
| \$ 1,922 | \$ 1,858 | \$ 7,654 | \$ -131 B | \$ 7,523 | 25.12¢ |
| 1,058 | 1,031 | 5,357 | -762 C | 4,595 | 15.34 |
| 878 | 850 | 4,022 | -910 D | 3,112 | 10.39 |
| \$ 3,858 | \$ 3,739 | \$17,033 | \$ -1,803 | \$15,230 | 50.85¢ |
| | | | | | |
| \$ 1,483 | \$ 1,199 | \$ 6,157 | \$ -400 E | \$ 5,757 | 19.22¢ |
| 568 | 558 | 2,820 | -20 F | 2,800 | 9.35 |
| 677 | 652 | 3,047 | -41 G | 3,006 | 10.04 |
| 1,065 | 952 | 4,535 | -212 H | 4,323 | 14.43 |
| 255 | 230 | 1,325 | -39 I | 1,286 | 4.29 |
| 898 | 658 | 3,722 | -411 J | 3,311 | 11.05 |
| 216 | 216 | 561 | - | 561 | 1.87 |
| \$ 5,162 | \$ 4,438 | \$22,167 | \$ -1,123 K | \$21,044 | 70.25¢ |
| 139 | - | 139 | -139 K | - | - |
| - | 10 | - | 61 L | 61 | 0.20 |
| - | - | - | 56 M | 56 | 0.19 |
| - | 8 | - | 37 N | 37 | 0.13 |
| - | -5 | - | -23 O | -23 | -0.08 |
| \$ 9,159 | \$ 8,190 | \$39,339 | \$ -2,934 | \$36,405 | 121.54¢ |
| | | | | | |
| \$ 2,303 | \$ 1,520 | \$ 5,779 | \$ -2,590 | \$ 3,189 | 10.64¢ |
| | | | | | |
| \$ - | \$ 29 | \$ - | \$ -116 P | \$ -116 | -0.38 |
| - | - | - | -794 Q | -794 | -2.65 |
| | | | | | |
| \$ 2,303 | \$ 1,549 | \$ 5,779 | \$ -3,500 | \$ 2,279 | 7.61¢ |

APPENDIX No. 2

Explanatory Notes

| | | |
|--|--|------------------|
| A. To offset incidental revenues against operating expenses: | | |
| Lodestar and Stinson rented to Inland in 1944 and 1945 | | 103,907 |
| DC-4 rented to United in 1947 | | 54,118 |
| Revenues from services to others in 1948 | | 186,000* |
| Total | | <u>\$344,025</u> |
| B. 1. Lodestar and Stinson costs in 1945 | | \$2,000 |
| 2. Training expense in 1946 related to Route 68. | | |
| DC-3 | | \$47,962 |
| DC-4 | | 40,003 |
| 3. Retroactive pilots' pay applicable to 1946 | | <u>\$63,224*</u> |
| 4. Retroactive pilots' pay transferred to 1946: | | |
| Eliminated from 1947 expense | | \$40,165 |
| Eliminated from 1948 expense | | 23,059 |
| | | <u>\$ 63,224</u> |
| 5. Excess of carrier's estimate over cost per hour | | |
| for last 6 months of 1948: | | |
| DC-3 at 38.61 per hour flown | | \$ 2,104 |
| DC-4 at 66.73 per hour flown | | 39,316 |
| | | <u>\$ 41,420</u> |
| Total | | <u>\$131,385</u> |
| C. 1. DC-3 overhaul expense in period in excess of amortiza- | | |
| tion of "built-in" and actual overhauls. | | \$ 2,197 |
| 2. To adjust reserve for aircraft and engine repairs: | | |
| DC-3 | | \$ 63,598 |
| DC-4 | | 79,853 |
| | | <u>\$143,451</u> |
| 3. Training expense in 1946 related to Route 68 | | \$ 38,139 |
| 4. Excessive DC-3 maintenance costs over 30.00 per hour: | | |
| 1946 | | \$290,775 |
| 1947 | | 160,911 |
| | | <u>\$451,686</u> |

*Denotes addition.

| | | |
|--|--|------------------|
| 5. Excess of carrier's estimate over constructive cost | | |
| per hour for last 6 months of 1948: | | |
| DC-3 at 16.99 per hour flown | | \$ 17,816 |
| DC-4 at 35.98 per hour flown | | 48,020 |
| | | <u>\$ 65,836</u> |
| 6. To eliminate costs of Stinson and Lodestar | | |
| Disallowed 1944-1947 | | 61,067 |
| Total | | <u>\$762,376</u> |

| | | | |
|----|---|------------|-----------|
| D. | 1. Extension of service life of DC-3 equipment | | \$224,985 |
| | 2. Excess equipment disallowed: | | |
| | Lodestar | \$44,900 | |
| | Stinson and AT-6's | 10,525 | |
| | DC-3 aircraft and engines | 62,623 | |
| | DC-4 aircraft and engines | 176,728 | \$294,776 |
| | 3. Depreciation on DC-3 "built-in" overhauls | | 59,243 |
| | 4. Excessive accrual of reserve for loss on retirement of non-rotatable spare parts and assemblies: | | |
| | Accrual on DC-3 parts | \$157,737 | |
| | Less: Allowance | 50,767 | |
| | Disallowance | | \$106,970 |
| | Accrual on DC-4 parts | \$281,271 | |
| | Less: Allowance | 200,000 | |
| | Disallowance | | 81,271 |
| | 5. Replacement of equipment by CV-240: | | \$188,241 |
| | DC-3 equipment | \$ 34,701 | |
| | DC-4 equipment | 62,172 | |
| | 6. Variance of carrier's estimate of CV-240 depreciation from allowance | | 96,873 |
| | Total | | \$45,396 |
| | | | \$909,514 |
| E. | 1. Pre-Operating costs in 1946 | | \$ 15,000 |
| | 2. Divestment costs applicable to Route 68: | | |
| | 1947 | \$101,000 | |
| | 1948 | 179,000 | |
| | 3. Offset of expenses applicable to incidental revenues | \$280,000 | |
| | 4. Wage increase for last half of 1948 | 125,000 | |
| | Total | 20,000* | |
| | | | \$400,000 |
| | 476 | | |
| F. | Divestment costs applicable to Route 68: | | |
| | 1947 | \$ 10,000 | |
| | 1948 | 10,000 | |
| | | | \$ 20,000 |
| G. | 1. Pre-operating costs of Route 68 in 1946 | \$ 15,000 | |
| | 2. Entertainment expense in 1947 | 1,000 | |
| | 3. Divestment costs applicable to Route 68 in 1948 | 25,000 | |
| | | | \$ 41,000 |
| H. | 1. Divestment costs applicable to Route 68: | | |
| | 1947 | \$ 72,000 | |
| | 1948 | 100,000 | |
| | 2. Wage increase last half of 1948 | 172,000 | |
| | 3. Offset of expenses applicable to incidental revenues | \$ 10,000* | |
| | Total | 50,000 | |
| | | | \$212,000 |

*Denotes addition.

| | | | |
|----|---|------|-----------|
| I. | 1. Contributions and entertainment expense: | | |
| | | 1945 | \$ 2,000 |
| | | 1946 | 6,000 |
| | | | <hr/> |
| | | | \$ 8,000 |
| | 2. Pre-operating expense applicable to Route 68 in 1946 | | \$ 6,000 |
| | 3. Divestment costs applicable to Route 68 in 1948 | | 25,000 |
| | | | <hr/> |
| | | | \$ 39,000 |
| J. | 1. Contributions and entertainment expense: | | |
| | | 1945 | \$ 20,000 |
| | | 1946 | 9,000 |
| | | 1947 | 14,000 |
| | | | <hr/> |
| | | | \$ 43,000 |
| | 2. Pre-operating expense applicable to Route 68 in 1946 | | \$ 12,000 |
| | 3. Additional allocation to Inland: | | |
| | | 1947 | \$ 18,000 |
| | | 1948 | 68,000 |
| | | | <hr/> |
| | | | \$ 86,000 |
| | 4. Divestment costs applicable to Route 68: | | |
| | | 1947 | \$ 98,000 |
| | | 1948 | 136,000 |
| | | | <hr/> |
| | | | \$234,000 |

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| | | |
|----|--|-----------|
| | 5. Offset of expenses applicable to incidental revenues | 36,000 |
| | | <hr/> |
| | Total | \$411,000 |
| K. | Allowance for wage increase included in functional accounts. | |
| L. | Amortization of pre-operating expense based on a 5-year period. | |
| | DC-4 aircraft and Route 68 | \$ 51,000 |
| | Convair 240 aircraft | 10,000 |
| | | <hr/> |
| | | \$ 61,000 |
| M. | Amortization of capitalized maintenance expense applicable to Route 68 based on a 5-year period. | |
| N. | Amortized on a 5-year basis. | |
| O. | Cash discounts treated as a credit to expense. | |
| P. | Net gain over past period after deducting losses. | |
| Q. | Profit from route sale considered "other revenue". | |

*Denotes addition.

*Operating Results for a Future Year
As Estimated by Western and as Adjusted by the Board*

| | Western Estimate ¹ | Adjusted Estimate Per Revenue Plane Mile |
|--|----------------------------------|---|
| | (000) | (000) |
| Non-Mail Revenues | | |
| Passenger | \$7,688 | \$7,688 123.95c |
| Express | 88 | 88 1.42 |
| Freight | 179 | 179 2.89 |
| Excess Baggage | 69 | 69 1.11 |
| Other | 260 | 110 A 1.77 |
| Total Non-Mail Revenue | \$8,284 | \$8,134 131.14c |
| Operating Expenses | | |
| Flying Operations | \$1,917 | \$1,875 B 30.23c |
| Direct Maintenance—Flight Equipment | 1,393 | 1,419 C 22.88 |
| Depreciation—Flight Equipment | 727 | 379 D 6.11 |
| Total Direct Expense | \$4,037 | \$3,673 59.12c |
| Ground Operations | \$1,476 | \$1,445 E 23.29c |
| Ground and Indirect Maintenance | 600 | 595 E 9.59 |
| Passenger Service | 763 | 763 12.30 |
| Traffic and Sales | 1,048 | 1,062 E 17.12 |
| Advertising and Publicity | 252 | 252 4.06 |
| General and Administrative | 1,070 | 870 E 14.03 |
| Depreciation—Ground Equipment | 220 | 220 3.55 |
| Total Ground and Indirect Expense | \$5,429 | \$5,207 E 83.94c |
| Provision for Wage and Price Increases | \$ 472 | \$ — F — |
| Amortization of CV-240 Pre- operating Expense | — | 30 G 0.48 |
| Amortization of Extension and Development Expense | — | 6 G 0.10 |
| Cash Discount Income | — | —5 H —0.08 |
| Total Operating Expense | \$9,938 | \$8,911 123.46c |
| Break-Even Need | \$1,654 | \$ 777 J 12.52c |

¹ It is intended that these data reflect the carrier's latest estimates.

APPENDIX No. 3

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Explanatory Notes

| | | |
|----|---|------------|
| A. | To offset incidental revenues against operating expenses pertaining thereto | \$150,000 |
| B. | Excess of carrier's estimate over cost of \$38.61 per DC-3 hour flown | \$ 42,243 |
| C. | Excess of carrier's estimate over cost of \$15.82 per DC-3 hour flown | 31,327 |
| | Wage and price increases | 57,000* |
| | | <hr/> |
| | | \$ 25,673* |
| | | \$141,757* |
| | | 75,292 |
| D. | 1. Extension of service life of DC-3's | |
| | 2. Replacement of DC-3's by Convair 240's | |
| | 3. Excess Equipment: | |
| | DC-4 aircraft and engines | 174,000 |
| | | <hr/> |
| | | \$177,315 |
| | 4. Excess of estimated accrual over allowance for loss on retirement of non-rotatable spare parts | \$ 5,250 |
| | 5. Depreciation on DC-3 built-in overhauls | 6,944 |
| | 6. Variance of carrier's estimate of Convair 240 depreciation from allowance | <hr/> |
| | | \$228,003 |
| | | <hr/> |
| | | \$347,732 |

Total

| Account | Offset Against Incidental Revenues | Wage and Price Increase | Excess Expense | Total |
|---------|---|-------------------------------|----------------------|-----------|
| 6100 | \$100,000 | \$ 69,000* | \$ — | \$ 31,000 |
| 6200 | 25,000 | 20,000* | — | 5,000 |
| 6400 | 20,000 | 34,000* | — | 14,000* |
| 6600 | 5,000 | 35,000* | 230,000 ¹ | 200,000 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| | \$150,000 | \$158,000* | \$230,000 | \$222,000 |

¹Includes additional allocation to Inland of \$84,000.

- F. Allowance of \$215,000 reflected in functional accounts; balance of \$241,000 not recognized.
 G. Amortized over a five-year period.
 H. Estimated from 1948 experience.

*Denotes addition.

*Operating Expenses per Revenue Ton Mile and Available
Ton Mile As Reported and As Adjusted*

| | 8 Months Ended For the Twelve Month Period Ended | | | | | Future Year |
|-------------------------------------|---|----------|----------|--------------------|----------|----------------|
| | 12-31-44 | 12-31-45 | 12-31-46 | 12-31-47 | 12-31-48 | |
| Per Rev. Ton Mile | | | | | | |
| Aircraft Oper. Expenses | | | | | | |
| As Reported | 18.81 | 22.58 | 25.27 | 28.42 | 32.72 | 26.19 |
| As Adjusted | 15.43 | 19.14 | 21.25 | 26.28 | 31.71 | 26.19 |
| Ground & Indir. Expenses | | | | | | |
| As Reported | 30.67 | 30.13 | 32.42 | 34.50 | 43.78 | 39.21 |
| As Adjusted | 30.67 | 29.92 | 32.08 | 32.70 | 37.64 | 36.47 |
| Total Oper. Expenses | | | | | | |
| As Reported | 49.48 | 52.71 | 57.68 | 62.92 | 77.78 | 71.78 |
| As Adjusted ¹ | 46.25 | 49.07 | 52.90 | 59.27 ² | 69.71 | 65.10 |
| Per Avail. Ton Mile | | | | | | |
| Aircraft Oper. Expenses | | | | | | |
| As Reported | 16.76 | 18.48 | 15.20 | 15.44 | 15.77 | 16.04 |
| As Adjusted | 13.76 | 15.67 | 12.78 | 14.28 | 15.28 | 14.41 |
| Ground & Indir. Expenses | | | | | | |
| As Reported | 27.33 | 24.67 | 19.51 | 18.74 | 21.10 | 21.57 |
| As Adjusted | 27.33 | 24.50 | 19.31 | 17.77 | 18.14 | 20.05 |
| Total Oper. Expenses | | | | | | |
| As Reported | 44.09 | 43.16 | 34.71 | 34.18 | 37.44 | 39.48 |
| As Adjusted ¹ | 41.21 | 40.18 | 31.83 | 31.19 ² | 33.60 | 35.81 |

¹Includes non-operating items for rate-making purposes.

²Does not reflect profit from sale of Route 68.

*Reported and Recognized Investment
For the Period May 1, 1944—December 31, 1948
(In Thousands)*

| | Average for the Eight Months Ended December 31, 1944 | | Average for the Twelve Months Ended December 31, 1945 | | Average for the Twelve Months Ended December 31, 1946 | | Average for the Twelve Months Ended December 31, 1947 | | December 31, 1948 | |
|---|--|------------|--|------------|--|------------|--|------------|-------------------|------------|
| | Reported | Recognized | Reported | Recognized | Reported | Recognized | Reported | Recognized | Reported | Recognized |
| Working Capital: | | | | | | | | | | |
| Current Assets | \$2,100 | | \$2,446 | | \$ 2,880 | | \$ 4,387 | | \$2,305 | |
| Prepayments and other Deferred Charges | 110 | | 283 | | 433 | | 530 | | 475 | |
| | | | | | | | | | | |
| Total | \$2,210 | | \$2,729 | | \$ 3,313 | | \$ 4,917 | | \$2,780 | |
| Current Liabilities | 1,410 | | 1,865 | | 4,779 | | 8,303 | | 2,757 | |
| Deferred Credits | 49 | | 130 | | 214 | | 263 | | 281 | |
| | | | | | | | | | | |
| Total | \$1,459 | | \$1,995 | | \$ 4,994 | | \$ 8,566 | | \$3,038 | |
| Net Working Capital | \$ 751 | | \$ 734 | | \$ (1,681) | | \$ (3,649) | | \$ (258) | |
| Investments and Spe- cial Funds | 438 | | 793 | 6B | 1,199 | 5B | 1,448 | 2 B | 718 | 2B |
| Operating Property and Equipment (Net) | 706 | 693C | 1,138 | 1,175C | 4,534 | 4,303 C | 7,247 | 6,263 C | 6,656 | 5,304C |
| Non-operating Property and Equipment (Net) | 3 | —D | 10 | —D | 23 | —D | 107 | —D | 190 | —D |
| Pre-Operating and Training Costs | — | — | — | — | — | 130E | — | 118 E | — | 73E |
| Capitalized | — | — | — | — | — | 139F | — | 150 F | — | — |
| Developmental Costs | — | — | — | — | — | — | — | — | — | — |
| Capitalized | — | — | — | — | — | — | — | — | — | — |
| Extension and Devel- opment | — | 13G | — | 12G | — | 41G | — | 15 G | — | 17G |
| | | | | | | | | | | |
| Total Investment | \$1,898 | \$1,463 | \$2,675 | \$1,927 | \$ 4,075 | \$4,717 | \$ 5,153 | \$6,079 | \$7,306 | \$5,842 |

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APPENDIX No. 5
Explanatory Notes

A.

| | 1946 | 1947 | 1948 |
|--|----------------|-----------------|-----------------|
| | (In Thousands) | | |
| Average Reported Short Term Notes Eliminated | \$(1,681) | \$(3,649) | \$(258) |
| | 1,652 | 2,833 | 227 |
| Pro-Rate with Inland | \$ (39) 28 | \$ (816) 7 | \$ (31) -90 |
| Add Retroactive Mail Pay | \$ (11) 150 | \$ (809) 340 | \$ (121) 567 |
| Adjusted Net Working Capital | \$ 139 | \$ (469) | \$ 446 |

B.

| | 1944 | 1945 | 1946 | 1947 | 1948 |
|---------------------------|----------------|-------|---------|---------|-------|
| | (In Thousands) | | | | |
| Average Reported | \$438 | \$793 | \$1,199 | \$1,448 | \$718 |
| Less: | | | | | |
| Investment in Affiliates | \$432 | \$474 | \$ 463 | \$ 428 | \$411 |
| Equipment Purchase Funds | — | 313 | 731 | 1,018 | 305 |
| Misc. Investments Allowed | \$ 6 | \$ 6 | \$ 5 | \$ 2 | \$ 2 |

C.

| | 1944 | 1945 | 1946 | 1947 | 1948 |
|--|----------------|-------|-------|-------|-------|
| | (In Thousands) | | | | |
| Average Reported | 706 | 1,178 | 4,534 | 7,237 | 6,656 |
| Elimination: | | | | | |
| Lodestar, Stinson, and AT-6 Aircraft | 32 | 20 | 12 | 3 | — |
| DC-3 Aircraft | 38 | — | 54 | 25 | — |
| Conversion Costs on DC-3 Aircraft | — | 173 | 50 | — | — |
| DC-3 Aircraft and Engines Replaced by CV-240 | — | — | — | — | 16 |
| DC-3 Aircraft and Spare Parts Allocated to Inland | — | — | 284 | 240 | 152 |
| DC-4 Cargo Aircraft | — | — | 125 | 198 | 146 |
| DC-4 Aircraft and Engines Replaced by CV-240 | — | — | — | — | 336 |
| Excess DC-4 Engines | — | — | 40 | 75 | — |
| Convair Engines and Spare Parts | — | — | — | 88 | 240 |
| Construction Work in Progress—Hangar | — | — | 52 | 374 | — |
| Allocation of Hangar Investment to Inland | — | — | — | 370 | 555 |
| Total Eliminations | 70 | 193 | 617 | 1,373 | 1,445 |
| Add: Increase in DC-3 Book Value Due to Extension of Service Life to 6-30-49 | 57 | 190 | 386 | 399 | 93 |
| Net Adjustment to Reported Operating Property | 13 | 3 | 231 | 974 | 1,352 |

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APPENDIX No. 5

- D. Property not used or useful for certificated operations.
 E. Average balance of costs capitalized as provided herein.
 F. Average balance of capitalized development costs related to Route 68 and offset against profit from sale on September 15, 1947.
 G. Capitalized extension and development costs accrued over period. Unamortized balance of \$26,058 applicable to Route 68 offset against profit from sale on September 15, 1947.

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APPENDIX No. 6

*Estimated and Recognized Investment
 For a Future Period
 (In Thousands)*

| | Western's Estimate 12-31-48 | Adjustments Recognized | |
|---|-----------------------------------|------------------------|---------|
| Working Capital: | | | |
| Current Assets | 1,397 | | |
| Prepayments and Other Deferred Charges | 600 | | |
| Total | 1,997 | | |
| Current Liabilities | 3,285 | | |
| Deferred Credits | 300 | | |
| Total | 3,585 | | |
| Net Working Capital | (1,588) | \$2,473 A | 885 |
| Investments and Special Funds | 404 | —396 B | 8 |
| Operating Property and Equipment (Net) | 8,137 | —2,121 C | 6,016 |
| Non-Operating Property and Equipment (Net) | 188 | —188 D | — |
| Pre-Operating and Training Cost Capitalized | — | 140 E | 140 |
| Extension and Development | — | 15 F | 15 |
| Total Investment | 7,141 | —77 | \$7,064 |

Explanatory Notes to Future Investment
(In Thousands)

| | | |
|----|--|-----------|
| A. | Working capital reported | \$(1,588) |
| | Allocation to Inland | 31 |
| | | <hr/> |
| | Add: Retroactive mail pay less income taxes | \$(1,619) |
| | | 680 |
| | | <hr/> |
| | Add: Notes payable eliminated from current liabilities | \$ (939) |
| | | 1,824 |
| | | <hr/> |
| | Working capital recognized for rate-making purposes | \$ 885 |
| | | <hr/> |
| B. | To eliminate investment in Inland. | |
| C. | Claimed operating property and equipment | \$ 8,137 |
| | Eliminations: | |
| | DC-3 equipment replaced by CV-240 | \$ 47 |
| | DC-3 equipment allocated to Inland | 106 |
| | DC-4 equipment replaced by CV-240 | 1,422 |
| | Investment in Los Angeles hangar | |
| | allocated to Inland | 546 |
| | | <hr/> |
| | Total Eliminations | \$ 2,121 |
| | | <hr/> |
| | Recognized operating property and equipment | \$ 6,016 |
| D. | Property not used or useful for certificated operations. | |
| E. | Capitalized costs related to inauguration of service with Convair 240's. | |
| F. | Unamortized balance of recognized extension and development expense. | |

APPENDIX No. 7

*Sliding Scale Mail Rates
at the Average Monthly Passenger Load Factors Indicated¹*

| Revenue Passenger Load Factor in Percent ² | Applicable Base Rate per Airplane Mile ³ |
|--|--|
| 54 | 33.00 |
| 55 | 31.60 |
| 56 | 30.20 |
| 57 | 28.80 |
| 58 | 27.40 |
| 59 | 26.00 |
| 60 | 24.60 |
| 61 | 23.20 |
| 62 | 21.80 |
| 63 | 20.40 |
| 64 | 19.00 |
| 65 | 17.60 |
| 66 | 16.20 |
| 67 | 14.80 |
| 68 | 13.40 |
| 69 | 12.00 |
| 70 | 10.60 |
| 71 | 9.20 |
| 72 | 8.40 |

¹ The passenger load factor is to be predicated upon a plane of 21 seats for miles flown with DC-3 type aircraft, of 40 seats for miles flown with Martin 202 or Convair 240 type aircraft, and of 50 seats for miles flown with four-engine type aircraft.

² After each of the figures in this column, the words "and fraction thereof" are to be understood.

³ When the passenger load factor is less than 55 percent, the maximum base rate of 33.00 cents per airplane mile will apply and when 72 percent or more the minimum base rate of 8.40 cents will apply.

Orders
Serial Number E-2333

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

487 ADOPTED BY THE CIVIL AERONAUTICS BOARD
 AT ITS OFFICES IN WASHINGTON, D. C.
 ON THE 30TH DAY OF DECEMBER, 1948

Docket No. 1374

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Order to Show Cause

The Board having considered all of the information and data set forth, or specifically referred to, in the Statement of Tentative Findings and Conclusions, together with the Appendices attached thereto, dated December 30, 1948 (hereinafter referred to as the "Statement"), which Statement is attached hereto and made a part hereof, and having on the basis thereof made the tentative findings and conclusions set forth in the Statement;

IT IS ORDERED, That Western Air Lines, Inc., is directed to show cause why the Board should not make final the findings and conclusions set forth in the Statement, and upon the basis thereof fix, determine, and publish the rates set forth in said Statement as the fair and reasonable rates of compensation to be paid the carrier for the transportation of mail by aircraft, the facilities used and

488 useful therefor, and the services connected therewith
over its routes within the continental United States
insofar as authorized by its certificates of public
convenience and necessity for interstate air transportation
and over its routes between the United States and terminal
points in Canada;

IT IS FURTHER ORDERED, That all further procedure herein shall be in accordance with Section 285.13 of the Economic Regulations and that any notice, as provided for in paragraph (c)(1) of said Section 285.13, that there exists any objection to the rates set forth in the Statement or to the admissibility in evidence of any exhibits accompanying, or to the information specifically referred to in, the Statement shall be filed with the Civil Aeronautics Board within ten days after the date of service of this Order, and if notice is filed as aforesaid, written answer and any supporting documents, as provided for in paragraphs (c)(1) and (c)(2) of said Section 285.13, shall be filed with the Board within thirty days after the date of service of this Order;

IT IS FURTHER ORDERED, That, if answer is filed hereto, all elements entering into the determination of a fair and reasonable rate, except insofar as limited in prehearing conference, shall be in issue, and in such event the final rate shall be determined upon the record made with respect to all issues stated in the prehearing conference report;

IT IS FURTHER ORDERED, That this order and the attached Statement of Tentative Findings and Conclusions be served upon Western Air Lines, Inc.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN, *Secretary*

(SEAL)

Orders
Serial Number E-2506

Feb. 25, 1949

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UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 25TH DAY OF FEBRUARY, 1949.

Docket No. 1374

In the matter of the compensation for the transportation of
mail by aircraft, the facilities used and useful therefor, and
the services connected therewith, of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar
as authorized under its certificates for interstate air trans-
portation and over its routes between the United States
and terminal points in Canada.

**Order Establishing Fair and Reasonable Temporary Rates
of Mail Compensation**

The Board heretofore having fixed, determined and pub-
lished fair and reasonable rates of compensation for the
transportation of mail from and after January 1, 1943, be-
tween the points between which Western Air Lines, Inc.
(hereinafter referred to as Western) was authorized to
transport mail by its certificates of public convenience and
necessity;¹

Western having on April 26, 1944, filed a petition request-
ing the Board to increase the mail rates so determined;

The Board, pursuant to amended petition filed by West-
ern, having fixed, determined and published a fair and
reasonable temporary mail rate for Western from and after

October 1, 1946,² and having further ordered that
555 this proceeding remain open pending entry of an

¹ *Western A. L., Mail Rates*, 4 C.A.B. 441 (1943).

² Order Serial No. E-484 (April 29, 1947).

order fixing and determining final fair and reasonable rates of compensation for such transportation of mail by aircraft, retroactive to such date as the Board may determine;

The Board having made a further analysis of Western's operating and financial results and reasonable requirements in connection with a determination of the final mail rates to be fixed for the carrier for the period May 1, 1944-December 31, 1948 (hereinafter referred to as the "past period") and for the period on and after January 1, 1949 (hereinafter referred to as the "future period");

The Board having issued a Statement of Tentative Findings and Conclusions and accompanying Order to Show Cause,³ proposing to establish final rates for the carrier both for the past period and the future period;

Western having filed an answer to the order to show cause accepting the final rate for the future period, raising certain legal objections to the rate proposed for the past period, and requesting that the rate proposed for the past period be fixed as a temporary rate;

The Postmaster General having filed a motion for leave to intervene in the proceedings, which was granted, and having filed an answer to the order to show cause and objections to the rates proposed by the Board for both the past period and the future period;

556 Western subsequently having filed a petition requesting the establishment of temporary rates for both the past and future periods in the same amounts and for the same periods as the rates proposed for Western in the Statement of Tentative Findings and Conclusions previously adopted by the Board;

Public hearing having been held in the above entitled matter on February 23, 1949;

THE BOARD FINDING THAT:

1. The analysis of Western's financial condition and reasonable requirements indicates that for both the past and future periods the final mail rates to be fixed may reasonably

³ Order Serial No. E-2333 (December 30, 1948).

be expected to be substantially in excess of the mail rates currently in effect for such periods;

2. The analysis also indicates that Western's financial condition is still critical and will deteriorate in the absence of provision increasing its mail compensation for both the past and future periods;

3. Final rates for the pertinent periods could not properly be established in time to provide Western with the immediate relief required and it will be in the public interest to establish temporary mail rates increasing mail compensation to Western for both the past and future periods;

4. The fair and reasonable temporary rates to be used as the basis for payment to Western for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith over its routes
557 within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada are in the amounts proposed in the Statement of Tentative Findings and Conclusions referred to above, as hereinafter set forth;

IT IS ORDERED THAT:

The fair and reasonable rates of compensation to be paid Western for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its routes within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada, are as follows:

(a) For the period beginning May 1, 1944, and ending December 31, 1948, the amount of \$4,252,000.⁴

(b) On and after January 1, 1949, for each month during which the average passenger load factor (computed in the manner set forth below) does not exceed 54.99 percent, a base rate of 33.00 cents per airplane mile; for each month

⁴ This amount of mail pay is equal to 14.20 cents per revenue plane mile flown in scheduled service.

during which the average passenger load factor exceeds 54.99 percent, a base rate per airplane mile which shall be less than 33.00 cents by 1.40 cents per airplane mile for each one percent, or fraction thereof, by which the average passenger load factor exceeds 54.99 percent, provided that

in no event shall the base rate per airplane mile be less than 8.40 cents; said average passenger load factor per month shall be computed to the nearest hundredth of one percent and shall be derived by dividing the total revenue passenger miles flown in scheduled passenger service during the month by the total seat miles operated during the month, the total seat miles to be derived by multiplying the number of miles operated in scheduled passenger service with each type of aircraft by the following standard number of seats established for purposes of this computation for such aircraft:

DC-3 type aircraft—21 seats; Convair 240 type aircraft—40 seats; All four-engine aircraft types—50 seats. said base rates, which are set forth in Appendix No. 1 hereof for each average passenger load factor, and the effective rates per airplane mile to be derived therefrom shall be paid on the mileage (without regard to any base poundage of mail) and under the terms herein stated, as follows:

(1) For each month during which the average daily scheduled mileage is not greater than the average daily designated mileage and does not exceed 16,300 miles, the appropriate base rate per airplane mile set forth in Appendix No. 1.

(2) For each month during which the average daily scheduled mileage exceeds the average daily designated mileage but does not exceed 16,300 miles, an effective rate per airplane mile (computed to the nearest hundredth of a cent) which bears the same relation to the appropriate base rate per airplane mile set forth in Appendix No. 1 as the average daily scheduled mileage bears to the average daily designated mileage.

(3) For each month during which the average daily scheduled mileage exceeds 16,300 miles, an effective rate

per airplane mile (computed to the nearest hundredth of a cent) which bears the same relation to the appropriate base rate per airplane mile set forth in Appendix No. 1 as 16,300 miles bears to the average daily designated mileage.

559 The aforesaid rates per airplane mile shall be applied to the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster General for the carriage of mail; provided, however, that if any scheduled flight is operated in two or more sections between any two points served for mail and mail is transported on more than one such section, the aggregate of the sections so used shall, for all purposes of computing compensation except the computation of the average passenger load factor, be treated as a single flight, and the rates shall be applied to the airport-to-airport mileage flown by that section which covers the greatest airport-to-airport mileage between points served for mail.

The average daily scheduled mileage shall consist of the mileage of all scheduled trips, exclusive of trips cancelled by management with a view to reducing the volume of service operated, and the average daily designated mileage shall consist of the mileages of all scheduled trips designated or ordered to be established by the Postmaster General for the carriage of mail; such mileages shall be computed as though the mileage of each trip were the airport-to-airport distance via all certificated points along the flight route between the terminals of each trip, with the exception that, on trips serving the points in the certificate of public convenience and necessity between the terminal point San Diego and the intermediate point Los Angeles on Route 13, the scheduled mileage and designated mileage of trips scheduled

(1) between San Diego and Yuma, (2) between 560 San Diego and Los Angeles, and (3) between Los Angeles and Palm Springs, shall be computed as though such mileage were the distance via the certificated stop points between the above named points in the sequence set forth for each trip in the carrier's schedules filed with

the Board. The average daily scheduled mileage and the average daily designated mileage shall be determined for each calendar month by taking the average (computed to the nearest mile) of the daily mileages of regularly scheduled trips, exclusive of trips cancelled by management with a view to reducing the volume of service operated, and of regularly designated trips, respectively, for the seven days of the week, without regard to any variations of scheduled or designated mileages, respectively, on holidays.

The compensation provided herein shall be inclusive of and not in addition to the mail compensation heretofore received by the carrier for mail transported on and after May 1, 1944.

IT IS FURTHER ORDERED, That the aforesaid order fixing fair and reasonable temporary rates shall be effective as of this date, all parties to the above-entitled proceeding having already waived all procedural requirements subsequent to hearing short of a final decision of the Board fixing temporary rates herein;

IT IS FURTHER ORDERED, That during the effectiveness of this order it shall supersede any prior inconsistent orders of the Board and shall govern the payment of compensation to Western for the transportation of mail by aircraft for the periods specified herein;

561 IT IS FURTHER ORDERED, That this proceeding remain open pending entry herein of an order fixing final rates for the period May 1, 1944-December 31, 1948, inclusive, and for the period on and after January 1, 1949, which said final rates may be lower or higher than the temporary rates fixed herein;

IT IS FURTHER ORDERED, That this order be served upon the parties herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN, *Secretary*

(SEAL)

*Sliding Scale Mail Rates
at the Average Monthly Passenger Load Factors Indicated¹*

| Revenue Passenger Load Factor in Percent ² | Applicable Base Rate per Airplane Mile ³ |
|--|--|
| 54 | 33.00 |
| 55 | 31.60 |
| 56 | 30.20 |
| 57 | 28.80 |
| 58 | 27.40 |
| 59 | 26.00 |
| 60 | 24.60 |
| 61 | 23.20 |
| 62 | 21.80 |
| 63 | 20.40 |
| 64 | 19.00 |
| 65 | 17.60 |
| 66 | 16.20 |
| 67 | 14.80 |
| 68 | 13.40 |
| 69 | 12.00 |
| 70 | 10.60 |
| 71 | 9.20 |
| 72 | 8.40 |

¹ The passenger load factor is to be predicated upon a plane of 21 seats for miles flown with DC-3 type aircraft, of 40 seats for miles flown with Martin 202 or Convair 240 type aircraft, and of 50 seats for miles flown with four-engine type aircraft.

² After each of the figures in this column, the words "and fraction thereof" are to be understood.

³ When the passenger load factor is less than 55 percent, the maximum base rate of 33.00 cents per airplane mile will apply and when 72 percent or more, the minimum base rate of 8.40 cents will apply.

* * * * * * * * *

Orders
Serial Number E-2531

571

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 3RD DAY OF MARCH, 1949.

Docket No. 1374

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Order Amending Order Establishing Temporary Rates of Mail Compensation

The Board having on February 25, 1949 issued an order (Serial No. E-2506) establishing fair and reasonable temporary rates of mail compensation for Western Air Lines, Inc., for the period May 1, 1944-December 31, 1948, and for the period on and after January 1, 1949;

Question having arisen concerning the construction of paragraph (a) and the accompanying footnote 4 to that paragraph of the order;

The Board finding it appropriate to resolve that question by amending the said order;

The Board further finding that the amendment of such order in the manner hereinafter set forth is required to effectuate the purposes thereof;

IT IS ORDERED, That Order Serial No. E-2506 be and it hereby is amended by striking out the sentence contained in

footnote 4 to paragraph (a) thereof and substituting therein the following:

572 This amount of mail pay is equal to approximately 14.20 cents per revenue plane miles flown in scheduled service during the period May 1, 1944, through December 31, 1948. While the Board is concerned with this entire period for rate-making purposes, administratively, the Post Office Department secures appropriations and keeps records of payments for the services in question on the basis of annual fiscal periods. For such administrative purposes alone, the Board finds, in the light of the data set forth in its Statement of Tentative Findings and Conclusions, that the amount of \$4,252,000 may be broken down into an amount of \$2,768,000 for the period May 1, 1944-December 31, 1947, which is equal to a rate of approximately 11.77 cents per revenue plane mile flown in scheduled service during this period; and an amount of \$1,484,000 for the calendar year 1948, which is equal to a rate of approximately 23.49 cents per revenue plane mile flown in scheduled service during such period.

IT IS FURTHER ORDERED, That this order shall be effective as of this date;

IT IS FURTHER ORDERED, That this order be served upon the parties herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN
M. C. MULLIGAN
Secretary

(Seal)

Orders

Serial Number E-2641

591

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICES IN WASHINGTON, D. C.
ON THE 28TH DAY OF MARCH, 1949.

Docket No. 1374

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

WESTERN AIR LINES, INC.

over its routes, within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Order Granting Motion For Severance

The Board having on December 30, 1948 issued a Statement of Tentative Findings and Conclusions and accompanying Order to Show Cause (Order Serial No. E-2333) proposing the mail rates specified therein for Western Air Lines, Inc. (hereinafter referred to as Western) for the period May 1, 1944-December 31, 1948 (hereinafter referred to as the past period) and for the period on and after January 1, 1949 (hereinafter referred to as the future period);

Notice of objection and Answer to certain aspects of the Statement and the Show Cause Order having been filed by Western and by the Postmaster General;

Western having filed a motion to sever the future period from the past period and having further requested that proceedings in connection with the mail rate for the
592 future period be expedited to pre-hearing conference;

The Postmaster General having filed objections to, and Public Counsel having filed a reply in support of, said motion;

Upon consideration of the foregoing and of the record, the Board finding that:

1. Failure to sever the future period from the past period will cause protracted delay in the establishment of a final rate for Western for the future for the reason, among others, that the answers of the Postmaster General and Western contain substantial objections to the mail rate proposed for past period, which is not the case as regards the rate proposed for the future period;

2. No grounds have been advanced warranting such delay;

3. The severance of the future period from the past period will expedite the establishment of a final mail rate for Western for the future period, and is conducive to the proper dispatch of business and to the ends of justice;

4. The elimination of delay in the establishment of a final rate for Western for the future period by the severance of such period from the past period is in the public interest.

IT IS ORDERED, That the motion of Western be and it hereby is granted and that the proceedings concerning the mail rate for Western for the period on and after January 1, 1949 be and they hereby are severed from the proceedings concerning the mail rate for the period May 1, 1944-December 31, 1948;

593 IT IS FURTHER ORDERED, That a copy of this order be served upon the parties herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

(Seal)

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Orders
Serial Number E-2848

651

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICES IN WASHINGTON, D. C.
ON THE 20TH DAY OF MAY, 1949.

Docket No. 2870

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.

over its entire system.

Docket No. 1374

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Order Consolidating Proceedings

Public Counsel having moved the Board to consolidate the above-entitled cases involving fair and reasonable mail rates for Inland Air Lines, Inc., and for Western Air Lines, Inc., for periods prior to January 1, 1949;

No objections to said motion having been filed by any party to these proceedings:

The Board finding that:

The conduct of these proceedings separately for Inland Air Lines, Inc., and for Western Air Lines, Inc., would in-

652 involve unnecessary duplication and result in a delay
 in the establishment of final mail rates for the car-
 riers for the reason that the nature of the matters
 involved in the Inland case are such that trial and determi-
 nation of the questions raised in the Western case will, in
 the absence of unforeseen developments, automatically
 govern the Inland case; and that consolidation of the above-
 entitled proceedings is, therefore, conducive to the proper
 dispatch of business and in the public interest.

IT IS ORDERED, That the above-entitled proceedings be and
 they are hereby consolidated, the consolidated proceeding
 to go forward under Docket No. 2870, Consolidated.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

(Seal)

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(Dec. 9, 1949)

904

BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.
Docket No. 1374

In the matter of the compensation of the transportation of
mail by aircraft, the facilities used and useful therefor, of
WESTERN AIR LINES, INC.

**Amendment No. 5 of
Petition of Western Air Lines, Inc.**

TO THE HONORABLE CIVIL AERONAUTICS BOARD:

Now comes Petitioner, Western Air Lines, Inc., and hereby further amends its Petition, as heretofore amended, in the above-entitled proceeding in the following particulars:

1. Paragraph 9 of the original petition as heretofore amended, is further amended by striking out, in the second paragraph of said paragraph 9, the clause "since the filing of the petition," and inserting in lieu of such clause, the words "since January 1, 1946".

2. Paragraph 11, inserted in the petition by Amendment No. 1, is further amended by striking out the clause "May 1, 1944, the date of the filing of this petition," and inserting in lieu of such clause the words "January 1, 1946".

3. The prayer of such petition, as heretofore amended, is hereby further amended insofar as said prayer relates to the filing of permanent air mail rates, so as to read as follows:

"Wherefore, Petitioner prays that a hearing be called and held as expeditiously as possible for the purpose
905 of fixing and determining the permanent air mail rate
for Petitioner in the amount alleged herein to be just
and reasonable, or such greater amount as may be found by

the Board to be just and reasonable under the circumstances, effective retroactively to January 1, 1946.”

Respectfully submitted,

WESTERN AIR LINES, INC.

By /s/ TERRELL C. DRINKWATER

TERRELL C. DRINKWATER

President

December 8, 1949

• • • • •

(Jan. 5, 1950)

909

UNITED STATES OF AMERICA
BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.

over its entire system, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Motion to Strike

Public Counsel moves the Board to strike "Amendment No. 5 of Petition of Western Air Lines, Inc." filed in the above-entitled proceeding on December 9, 1949, and in support of this motion respectfully shows the Board as follows:

On April 26, 1944 Western Air Lines, Inc. (Western) filed a petition with the Board requesting an increase in its then current rate of mail compensation. In the petition and various amendments thereto Western prayed the Board to make the requested mail rate effective as of May 1, 1944.¹

¹ See, e.g., p. 4 of the petition, and paragraph 11 of Amendment No. 1 to the petition, filed on February 10, 1947:

"Problems confronting Petitioner require that a permanent mail rate in response to this petition be determined and fixed as expeditiously as possible and *be made retroactive to May 1, 1944* the date of the filing of this petition * * *." [Emphasis supplied].

Since the petition was filed only four days prior to May 1, 1944, that date has consistently been considered as the filing date for rate making purposes.

In its Tentative Statement and accompanying Show Cause Order adopted for Western on December 30, 1948, (Order Serial No. E-2333), the Board determined that the mail rate therein proposed should commence as of the date of the carrier's petition, May 1, 1944. The Statement, at pages 4 and 5, detailed the reasons for the Board's tentative conclusion that the rate making period should commence as of May 1, 1944 rather than some later period.

The Board's Show Cause Order proposing the permanent rate for the period May 1, 1944—December 31, 1948 was contested by both the carrier and the Postmaster General. In view of the fact that it appeared that proceedings on the Show Cause Order would not be completed in the immediate future, in response to Western's petition the Board issued an order on February 25, 1949 establishing a temporary mail rate for Western for the past period in the total amount of \$4,252,000. This temporary mail rate was for the entire period May 1, 1944—December 31, 1948.

The proceedings in connection with the permanent mail rate for the period May 1, 1944—December 31, 1948 were set for prehearing conference before an Examiner of the Board.² During the course of the prehearing conference the carrier asserted that the rate should be made effective for the period January 1, 1946—December 31, 1948, rather than for the entire period commencing with the date of the filing of its petition. Accordingly, it raised as an issue in this proceeding the propriety of the rate making period prescribed in the Show Cause Order. This is disclosed clearly at page 6 of the statement of issues in the report of the Examiner, served on July 1, 1949, where issue 6(a) is set forth as follows:

“For what period shall mail rates be established for Western in this proceeding:

² These proceedings (Docket No. 1374) were consolidated by order of the Board with a similar rate proceeding for Western's subsidiary, Inland Air Lines, Inc., the consolidated proceeding being assigned Docket No. 2870, Consolidated.

- (1) May 1, 1944—December 31, 1948.
- (2) January 1, 1946—December 31, 1948.
- (3) Another portion of the period May 1, 1944—December 31, 1948."

The positions of the parties as to this issue also appear at the same page of the Examiner's report, as follows:

"Public Counsel and the Post Office agree that rates should be established for May 1, 1944—December 31, 1948. The carrier contends for January 1, 1946—December 31, 1948."

Subsequent to the issuance of the Examiner's report, voluminous written exhibits were exchanged by the parties. The exhibits, in part, were addressed to the issue of the appropriate rate making period as set forth in the Examiner's report. The Board's decision on that issue obviously should be made in context with the facts developed in the exhibits and at the hearing and upon consideration of the briefs of the parties and oral argument before the

Board.³ The hearing before the Examiner was commenced on December 12, 1949, and will not be concluded until about mid-January of 1950.

Amendment No. 5 to the petition, which is the subject of this motion, purports (1) to amend the April 26, 1944, petition of Western so as to request determination by the Board of a permanent mail rate for the carrier for the period on and after January 1, 1946 and (2) to exclude from the Board's consideration the period from May 1, 1944 through December 31, 1945. Amendment No. 5 was apparently filed in an attempt to oust from the jurisdiction of the Board the question of the proper rate making period—an important issue in this proceeding, which is currently being tried at the hearing in this case. In other words, by

³ As appears under issue No. 6 as set forth in the Examiner's report, it is the carrier's position that in the light of all of the *circumstances* the rate making period should not commence as of May 1, 1944. Testimony with regard to such circumstances has been introduced by the carrier at the hearing as part of its direct case.

the filing of Amendment No. 5, Western apparently seeks to preclude the Board from considering the rate making period issue on the merits.

No citation of authority is necessary to support the principle that by the lodging of Amendment No. 5 Western cannot foreclose the Board from considering on the merits the issue of the appropriate rate making period, as framed at the prehearing conference and in the Examiner's report, upon conclusion of the hearing and after briefs and oral argument before the Board.⁴ The Board has adopted a tentative conclusion as to the rate making period issue; the question of the appropriate rate period was framed as an issue in this proceeding; the parties have taken positions thereon; and the matter is currently the subject of 913 testimony in the hearing. Clearly, to the extent that

Western contends for a rate period commencing as of a date other than May 1, 1944, such contention must be determined by the Board in the light of the record, upon conclusion of the hearing and further appropriate proceedings. In effect, Western's Amendment No. 5 attempts to usurp the Board's functions, since if that Amendment is of legal effect and is permitted to stand, Western itself will have decided its own contention as to the appropriate rate making period in its own favor. As the administrative agency charged with the duty of making such determinations, the Board obviously cannot brook such an interference with the discharge of its responsibilities.

While it is the view of Public Counsel that there is no authority for the filing of this amendment, and that, in any event, it is of no legal effect, its very pendency at this time is prejudicial to the various parties. It is possible that the pendency of Amendment No. 5, without formal action by the Board indicating that it is of no legal effect, might be urged by Western as an argument at some future date to estop the Board from passing upon the merits of the rate

⁴ Indeed, in an earlier proceeding concerning Western, the Board articulated that principle and applied it. Cf. *Western Air Lines, Inc., Mail Rates for Routes Nos. 13, 19, and 52*, 4 C.A.B. 441, 442 (1943).

making period question now being tried in this case. The transcript of the hearing before the Examiner, to this point, will disclose that the lodging of the amendment has already resulted in much confusion.

Accordingly, Public Counsel respectfully requests that the Board strike Amendment No. 5 and that such action by the Board be taken at the earliest possible date so that the

914 Board's later determination of the rate making period issue will proceed on the merits after orderly conclusion of the hearing in this proceeding.

Respectfully submitted

/s/ HARRY H. SCHNEIDER
HARRY H. SCHNEIDER
Public Counsel

January 5, 1950

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(Jan. 26, 1950)

921

BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 et al.

In the Matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.

over its entire system, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Answer of Western Air Lines, Inc., to Public Counsel's Motion to Strike

TO THE CIVIL AERONAUTICS BOARD:

Now comes Western Air Lines, Inc., and opposes Public Counsel's Motion to Strike Amendment No. 5 of Western Air Lines' Petition in the above-entitled proceeding and requests that such motion be denied. In support thereof Western Air Lines states the following:

1. The basic contention made by Public Counsel in support of his Motion to Strike is that since at the prehearing conference one of the issues framed was the determination of the proper initial date for the beginning of the rate-making period, Western cannot later preclude the Board from exercising its discretion to determine the proper date. Western submits that the problem presented by its Amendment No. 5 is not so simple as Public Counsel states
922 it—something more is involved than the procedural question whether an issue once stated can be later eliminated from the case by one party. On the contrary, the

basic limitations on the Board's rate-making jurisdiction are brought into operation by Western's Amendment No. 5.

2. This rate proceeding was instituted, not by the Board, but by the filing by Western on April 26, 1944, of a Petition seeking a limited review of its mail rates. The filing of the Petition was a voluntary act by Western, and in its Petition Western asked only for an *increase* in rates. There is nothing in the law which denies to Western the right to now amend its limited petition with respect to the period prior to January 1, 1946—and Western has done so.

3. Public Counsel suggests that Amendment No. 5 can have no effect on the scope of the proceeding. But no action was taken by the Board in the proceeding nor was an order of any kind issued until the Board's order dated April 29, 1947, fixing temporary rates for a period beginning October 1, 1946. The principal is now firmly established that the Board is without power to make a readjustment of rates (fixed by it in a prior final decision) with respect to a period prior to the date on which such readjustment of rates is put in issues, *Transcontinental & Western Air, Inc. Civil Aeronautics Board*, 336 U.S. 601 (1949); *Capital Airlines, Inc. v. Civil Aeronautics Board*, 171 F. 2d 339 (C.A. D.C.-1948). In the present case, the Board did not issue any order prior to January 1, 1946, which had the effect of instituting a general rate review on its own initiative. The only proposition upon which the Board could rest its retroactive review of Western's rates for the period prior to January 1, 1946, was Western's original petition—but that petition insofar as it relates to that period has been withdrawn by Western's Amendment No. 5. For the Board now to retroactively review Western's rates for the period prior to January 1, 1946, would violate the jurisdictional limitations defined by the *TWA* and *Capital* cases.

4. While not essential to reaching the above conclusion, the soundness of that conclusion is made still clearer by the fact that Western's original Petition did not ask for
 923 a general review of rates, but was expressly limited to a prayer for an *increase* in rates. The Board, how-

ever, now seeks to *reduce* the rates for the 1944-45 period, without having effectively broadened the issues at or prior to the beginning of that period. The Board cannot base a retroactive reduction on a petition for increase now withdrawn.¹

5. It cannot be maintained here, even if it were pertinent to the legal question involved, that Western has forfeited its right to file Amendment No. 5 because it has misled the Board into refraining from instituting a proceeding on the Board's initiative. Early in its existence, the Board established the practice of instituting broad rate proceedings on its own initiative, in order to fix an early beginning for the review period, whenever it felt that a carrier's rates might need a general review.² The Board has done this even where the carrier has had on file at the time a rate petition of its own.³ Thus the Board by consistent administrative practice has recognized as an inherent limitation of its rate-making jurisdiction the fact that if it wanted to be assured of the pendency of a rate proceeding having an adequate scope for review of a particular carrier's rates, it was necessary that the Board issue its own initiating order at the beginning of the period sought to be covered.

924 In the face of this demonstrated awareness by the Board of the procedural problem, it cannot be said that the Board's failure to issue, during 1944 and 1945, an order instituting a general rate proceeding for Western sprang from its reliance upon Western's very limited rate

¹ Note the Board's recognition of this general problem in *American Airlines, Inc., Mail Rate Proceeding*, 3 C.A.B. 323, at page 331.

² *Eastern Airlines, Mail Rates*, 3 C.A.B. 733; *American Airlines, Mail Rates*, 3 C.A.B. 323; *Chicago & Southern Air Lines, Mail Rates*, 3 C.A.B. 161; *Pennsylvania Central Airlines, Mail Rates*, 4 C.A.B. 22. Following the adoption of the Show Cause Order procedure, the Board frequently used such orders as initiating orders to secure rate reduction for the period beginning on or after the date of issuance of the order, for example, *Chicago & Southern Air Lines, Mail Rates*, 4 C.A.B. 419 and 529. Note also the Board's careful framing of the scope of the issues by its initiating orders in *Pan American Airways, Transatlantic Mail Rates*, 7 C.A.B. 605.

³ *American Airlines, Mail Rates*, supra note 2; *Transcontinental & Western Air, Mail Rates*, 4 C.A.B. 139; *American Overseas Airlines, Mail Rates*, 7 C.A.B. 623.

petition as supplying the Board's jurisdiction to make a broad general review of rates.

On the contrary, the plain fact of the matter is that in accordance with the policies and principles then being followed by the Board, as incorporated by it in its so-called .3 mill rate cases of 1942 and 1943, the .3 mill rate received by Western throughout 1944 and 1945 was not then regarded by the Board as excessive. A comparison of Western's actual reported operating profit for 1944 and 1945 shows that it was close to that which the Board estimated would accrue to Western in its opinion fixing Western's .3 mill rate (4 C.A.B. 441, decided November 8, 1943). Such thinking as may now exist within the Board that Western's rates in 1944 and 1945 were too high is obviously of recent origin—and it is that fact which is responsible for the Board's failure here to institute by its own order a general rate review proceeding in seasonable time.

WHEREFORE, Western Air Lines, Inc., submits that the Motion to Strike filed by Public Counsel should be denied. Western further submits that the Board is without power to grant the Motion, and should it do so, the granting of the Motion would be without legal effect.

Respectfully submitted,

WESTERN AIR LINES, INC.

D. P. RENDA

D. P. RENDA

Attorney for Western Air Lines, Inc.

January 24, 1950

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Orders
Serial Number E-3972

Mar 9—1950

927

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 9TH DAY OF MARCH, 1950.

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.
over its entire system, and of

WESTERN AIR LINES, INC.
over its routes within the continental United States insofar as authorized under its certificates for interstate transportation and over its routes between the United States and terminal points in Canada.

Order on Motion to Strike

Western Air Lines, Inc. (Western), having on December 9, 1949 transmitted for filing with the Board a document entitled "Amendment No. 5 of Petition of Western Air Lines, Inc.", which purports to amend its mail rate petition of April 26, 1944 so as to substitute for the date of filing of such petition the date January 1, 1946;

Public Counsel having on January 5, 1950 filed a motion, accompanied by supporting reasons, to strike said document and the Postmaster General having on January 9, 1950 filed a memorandum in support of said motion;

928 Answer to the motion having been filed by Western on January 26, 1950;

The Board, after due consideration of all the matters set forth in "Amendment No. 5," the motion and supporting memorandum, and the answer of Western, as well as of all other matters of record, finding that:

1. The Statement of Tentative Findings and Conclusions and accompanying Show Cause Order for Western (Order Serial No. E-2333), adopted by the Board in this proceeding on December 30, 1948, proposed to establish a final mail rate for Western for the period commencing May 1, 1944, and terminating December 31, 1948;

2. Formal objection having been made to said Statement and Show Cause Order in various respects, proceedings herein are being conducted pursuant to Section 302.13 (e) of the Procedural Regulations.

3. In accordance with the procedural regulations, issue as to the rate-making period proposed in the Statement was raised by Western, the carrier contending that the rate period should commence as of January 1, 1946 and both Public Counsel and the Postmaster General contending that the period should be established as of May 1, 1944;

4. Hearing as to such issue has already been conducted and concluded before an examiner of the Board;

5. The issue so raised must be determined by the Board on the merits, on the basis of the record made as to such issue, including the exhibits and transcript of hearing as well as the briefs and oral argument of the parties;

929 6. Western requested and has obtained, by virtue of Order Serial No. E-2506 of February 25, 1949, temporary mail pay for the entire period from May 1, 1944 through December 31, 1948;

7. The amendment to which the motion to strike is addressed would, if effective, remove the issue of the appropriate rate-making period from this proceeding by unilateral action of Western and deprive the parties of the right to be heard on the merits of that issue;

8. The amendment, if effective, would interfere with the authority of the Board to pass upon the merits of that issue;

9. Under the foregoing circumstances, the amendment purported to be made by Western could not be effected properly without prior consent of the Board granted after request for leave to file such amendment;

10. Treating the purported amendment as containing a request by Western for leave to file such amendment, leave should not be granted because the granting thereof would be prejudicial to the parties and contrary to the public interest;

11. The amendment should, accordingly, be rejected and be deemed without effect, and leave to file such amendment should not be granted;

IT IS ORDERED, That the motion to strike "Amendment No. 5" of Western be and it hereby is granted by rejecting said Amendment No. 5;

IT IS FURTHER ORDERED, That treating the amendment as including a request for leave to file such amendment, the request be and it hereby is denied.

930 IT IS FURTHER ORDERED, That this Order be and it hereby is without prejudice to the right of all parties to a determination by the Board on the merits of the issue of the appropriate rate-making period to be established in this proceeding.

IT IS FURTHER ORDERED, That this order shall be effective as of this date.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN
M. C. MULLIGAN
Secretary

(Seal)

• • • • •

Exhibit No. W12**WESTERN AIR LINES, INC.****LEASE***Parties*

CITY OF LAS VEGAS, a Municipal Corporation of the State of Nevada, referred to as "Lessor",

and

WESTERN AIR LINES, INC., a corporation organized under the laws of the State of Delaware, referred to as "Lessee."

Recitals

A. Lessor owns and operates at Las Vegas, Nevada, a municipal airport known as "McCarran Field", located near the City of Las Vegas, County of Clark, State of Nevada.

B. As of August 1, 1942, Lessor and Lessee entered into a lease under which Lessee herein and therein has certain rights and privileges with respect to the airport and the administration building located thereon.

C. Without impairing and, except as in this lease expressly provided, without affecting the lease between the parties dated August 1, 1942, Lessor desires to lease to Lessee additional space in the administration building, and desires to grant to Lessee additional rights and privileges with respect to the administration building in consideration of the assumption by Lessee of certain duties and obligations imposed upon Lessor under the lease dated August 1, 1942.

Terms

1. Lessor leases to Lessee the following premises and grants to Lessee the following rights and privileges:

(a) The space in the administration building designed for use as a restaurant or coffee shop, together with all other spaces in or about the administration building and the wait-

ing room designed or adaptable for use by concessionaires in connection with the sale of beverages, food, refreshments, magazines, newspapers, tobacco, drugs, curios, notions, novelties, and other articles or items which lend themselves for sale or display in an airline terminal;

(b) The exclusive right to maintain and operate in and about the administration building and the waiting room, a restaurant or coffee shop and booths or concessions for dispensing beverages, food, refreshments, magazines, newspapers, tobacco, drugs, curios, notions, novelties, and other articles or items which lend themselves for sale or display in an airline terminal;

(c) The exclusive right to maintain and operate in and about the administration building and the waiting room coin slot machines and other similar coin operated machines;

(d) The exclusive rights granted Lessee in paragraphs (b) and (c) above shall not prevent the Armed Forces of the United States from enjoying similar rights on premises used or occupied exclusively by such Armed Forces.

2. In addition to the obligations undertaken by Lessee under this lease, Lessee shall pay to Lessor as rental the sum of One Hundred (\$100.00) Dollars per month, payable monthly at the end of each month.

3. Lessee agrees to provide, at its expense, reasonable janitor service for the administration building as presently constructed, including customary and reasonable consumable supplies and facilities required to keep and maintain the administration building in a clean, orderly, sanitary and presentable condition.

4. Lessee shall pay for all electricity required to light the inside and outside of the present administration building, except the space or spaces occupied by governmental agencies, including, without limitation, the Civil Aeronautics Administration and the United States Weather Bureau; and Lessee shall operate the heating and cooling

systems and shall pay for the electric power and fuel required therefor and for the electric power required for the operation by Lessee of the restaurant or coffee shop and the other concessions covered by this lease.

5. Lessee, at its expense, shall furnish the equipment, fixtures, and facilities deemed by it necessary to operate the restaurant or coffee shop and to operate the other concessions which will be operated by Lessee under this Lease.

6. Lessor, at its expense, shall install complete and adequate heating and cooling systems in the administration building, and furnish and install adequate, serviceable, and attractive furniture and furnishings for the waiting room and all necessary fixtures and permanent facilities for the public rooms in the administration building, including, without limitation, a refrigerated drinking fountain, toilet paper dispensers, paper hand towel dispensers, soap dispensers, mirrors, and waste paper or rubbish containers; and Lessor agrees to replace, repair, or refinish all of such items whenever necessary in order to maintain them in an attractive, orderly, and serviceable condition.

7. Lessor will maintain in good order and repair the structure, the roof, the outer and inner walls, doors, windows, entrances, and plumbing facilities (except plumbing facilities installed by Lessee) of the administration building, and will make such repairs thereto or repainting or refinishing thereof as may be necessary from time to time to preserve and maintain the administration building in a serviceable and attractive condition.

8. In connection with its rights and duties under this lease, Lessee shall have the right to establish and enforce reasonable rules and regulations.

9. Lessor will impose no license, fee, or other charge upon Lessee for the right to conduct, maintain, and operate the restaurant or coffee shop and the concessions covered
2505 by this lease, other than the rental required to be paid and the obligations assumed by Lessee here-

under, or other than usual licenses or fees imposed on like businesses in the City of Las Vegas.

10. All fixtures, equipment, facilities, supplies, and merchandise purchased by Lessee and placed or installed in or about the administration building pursuant to this lease, however, affixed or installed, shall remain the property of Lessee, and shall be removable by Lessee at any time during the existence of this lease, or any renewal, and within thirty (30) days after the termination hereof, provided, however that any damage caused to the walls, ceiling, roof, or floor of said building by the removal of any of said fixtures, equipment, facilities, supplies and merchandise shall be immediately repaired by and at the expense of the Lessee.

11. In the event Lessee's operations should be taken over by the United States Government, or in the event Lessee should discontinue its commercial airline operations in and out of Las Vegas, Nevada, or in the event all commercial airline operations should be transferred to another airport in the Las Vegas area, Lessee, at its option, may suspend all of its obligations hereunder during the continuance of such condition upon giving to Lessor thirty (30) days' notice in writing of its intention so to do; provided, in the event such suspension shall remain in effect for a period of one year, Lessor at its option, may terminate this lease upon giving to Lessee thirty (30) days' notice in writing of its intention so to do; and provided further that the period of such suspension shall be added to the term of this lease by way of an automatic extension, unless the suspension period shall continue beyond one year followed by a termination of this lease under Lessor's option.

12. In the event the administration building shall be destroyed or shall be damaged to the extent that Lessee cannot reasonably, profitably, and practicably operate a restaurant or coffee shop and the concessions and slot machines covered hereby, all obligations of Lessee hereunder shall be suspended until a new administration building shall have been constructed by Lessor or until the damages shall

have been repaired, and the period of such suspension shall be added to the term of this lease by way of an automatic extension.

13. In the event it shall become illegal for Lessee to operate any of the concessions or the slot machines referred to herein in the administration building, the rental shall be reduced by mutual agreement to an amount not exceeding Fifty (\$50.00) Dollars per month during the period that Lessee shall not be able to operate the concessions or slot machines; and, in the event such period shall continue for three (3) months, Lessee, at its option, may terminate this lease upon giving to Lessor thirty (30) days' notice in writing of its intention so to do.

14. This lease is independent of the lease between the parties dated August 1, 1942, but so long as this lease shall remain in full force and effect any term, condition, or provision of this lease which is specifically in conflict with any term, condition, or provision of the lease dated August 1, 1942, the term, condition, or provision in this lease shall prevail and the conflicting term, condition, or provision in the lease dated August 1, 1942, shall remain in suspension; provided that upon the termination of this lease the
2506 suspended term, condition, or provision in the lease dated August 1, 1942, shall be revived.

15. The term of this lease shall be ten (10) years from the date hereof, and Lessee shall have the option of extending this lease for an additional period of five (5) years on the same conditions and at the same rental provided Lessee shall give to Lessor written notice of its election so to do not less than thirty (30) days prior to the expiration of the ten-year term.

16. In the event either Lessor or Lessee shall become in default hereunder, this lease may be cancelled at the option of the non-defaulting party upon giving to the defaulting party thirty (30) days' notice in writing of its intention so to do, unless within the thirty (30) days' period the defaulting party shall cure the default.

17. Any notices required or desired to be given to Lessor may be served by registered mail, postage prepaid, addressed to the City Clerk of the City of Las Vegas, Las Vegas, Nevada; and any notices required or desired to be given to Lessee may be served by registered mail, postage prepaid, addressed to Lessee at Burbank, California, or at such other address that Lessee may designate hereafter in writing.

18. This lease shall be deemed to be made in and construed under the laws of the State of Nevada.

Executed in duplicate original this 16th day of March, 1943.

THE CITY OF LAS VEGAS
By /s/ HOWELL C. GARRISON
Its Mayor

LESSOR.

WESTERN AIR LINES, INC.
By /s/ L. H. DWERLKOTTE
Its Vice President

LESSEE.

Attest:

/s/ Helen Scott Reed
City Clerk

(Seal)

Attest:

/s/ Paul E. Sullivan
Secretary

(Seal)

Exhibit No. W-14

2519

WESTERN AIR LINES, INC.

SUMMARY OF PROFIT OR LOSS FROM OPERATION OF
RESTAURANTS, CANTEENS AND COIN VENDING MACHINES
YEARS 1944 THROUGH 1948

| | Restaurants | Coin Vending Machines | Canteens | Total |
|---------------------------------------|--------------|--------------------------|-----------|------------|
| 1947 | \$(9,186.08) | 22,156.60 | 2,601.19 | 15,571.71 |
| 1946 | 5,186.81 | 29,909.70 | 6,605.70 | 41,702.21 |
| 1945 | 22,513.88 | 31,831.42 | 3,062.70 | 57,408.00 |
| 1944—May through December | (2,101.90) | 17,877.98 | 788.90 | 16,564.98 |
| Total included in Show Cause Order | 16,412.71 | 101,775.70 | 13,058.49 | 131,246.90 |
| Add: 1948 | (11,761.92) | 7,840.70 | 754.89 | (3,166.33) |
| Total 1944-1948 | \$4,650.79 | 109,616.40 | 13,813.38 | 128,080.57 |

() Denotes Loss

SOURCE: WAL Company Records.

2520

WESTERN AIR LINES, INC.

PROFIT OR LOSS FROM RESTAURANT OPERATIONS
YEARS 1944 THROUGH 1948

| | Las Vegas | Salt Lake City | Long Beach | Total |
|---------------------------------------|---------------|-------------------|-------------|------------|
| 1947 | \$(6,066.62) | (3,119.46) | — | (9,186.08) |
| 1946—(Note 1) | (6,486.20) | 15,229.95 | (3,556.94) | 5,186.81 |
| 1945 | (3,965.90) | 29,889.99 | (3,410.21) | 22,513.88 |
| 1944—May through December | (5,032.15) | 6,165.08 | (3,234.83) | (2,101.90) |
| Total included in Show Cause Order | (21,550.87) | 48,165.56 | (10,201.98) | 16,412.71 |
| Add: | | | | |
| Total 1944-1948 | \$(29,660.26) | 44,513.03 | (10,201.98) | 4,650.79 |

() Denotes Loss

Note 1—Long Beach operated thru May, 1946

Note 2—Salt Lake Operated thru April, 1948

SOURCE: WAL Company Records.

2521

WESTERN AIR LINES, INC.

PROFIT OR LOSS FROM OPERATION OF CANTEENS
YEARS 1944 THROUGH 1948

| | Las Vegas | Salt Lake City | Long Beach | Total |
|---------------------------------------|------------|-------------------|------------|-------------|
| 1947 | \$ 708.35 | 1,892.84 | — | 2,601.19 |
| 1946 | 1,760.80 | 5,129.96 | (285.06) | 6,605.70 |
| 1945 | 76.52 | 3,714.83 | (728.65) | 3,062.70 |
| 1944—May through December | (167.13) | 1,663.45 | (707.42) | 788.90 |
| Total included in Show Cause Order | 2,378.54 | 12,401.08 | (1,721.13) | 13,058.49 |
| Add: | | | | |
| 1948 | 804.86 | (49.97) | — | 754.89 |
| 1948—(Note 2) | (8,109.39) | (3,652.53) | — | (11,761.92) |
| Total 1944-1948 | \$3,183.40 | 12,351.11 | (1,721.13) | 13,813.38 |

() Denotes Loss

Note: Canteen operations included sales of Candy, Tobacco, Newspapers and Periodicals, Souvenirs, etc.

SOURCE: WAL Company Records.

2522

WESTERN AIR LINES, INC.

PROFIT OR LOSS FROM COIN VENDING MACHINES
YEARS 1944 THROUGH 1948

| | Las Vegas | Salt Lake City | Long Beach | Total |
|---------------------------------------|-------------|-------------------|------------|------------|
| 1947 | \$15,671.45 | 6,485.15 | — | 22,156.60 |
| 1946 | 24,697.25 | 5,212.45 | — | 29,909.70 |
| 1945 | 26,397.11 | 5,434.31 | — | 31,831.42 |
| 1944—May through December | 14,128.11 | 3,637.72 | 112.15 | 17,877.98 |
| Total included in Show Cause Order | 80,893.92 | 20,769.63 | 112.15 | 101,775.70 |
| Add: | | | | |
| 1948 | 6,048.50 | 1,792.20 | — | 7,840.70 |
| Total 1944-1948 | \$86,942.42 | 22,571.83 | 112.15 | 109,616.40 |

SOURCE: WAL Company Records.

* * * * *

Exhibit No. WX-3

2827

Date 12/15/49

WESTERN AIR LINES, INC.

Western-Inland Mail Rate Proceeding

Docket No. 2870 et al.

NOTICE—INVITATION TO NEGOTIATE
DECEMBER 28, 1942

The Board of City Commissioners are desirous of opening negotiations with interested parties on or before the 16th of January, 1943, for a lease of the coffee shop and other concessions in the Municipal Airport Administration Building. Contact city clerk.

HELEN SCOTT REED,
City Clerk

2828

Exhibit No. WX-4

Date 12/15/49

WESTERN AIR LINES, INC.

Western-Inland Mail Rate Proceedings

Docket No. 2870 et al.

February 17, 1943

MR. C. R. CLARK
1017 Frances Street
Las Vegas, Nevada

Dear Mr. Clark:

The undersigned, Western Air Lines, Inc., a Delaware corporation, hereby submits the following bid for leasing that certain space in the McCarran Field Airport Administration Building owned by the City of Las Vegas, which was designed for use as a coffee shop of approximately 30 feet by 32 feet, or approximately 960 square feet, and the

right to place coin slot machines in said Administration Building.

1. Western Air Lines, Inc. proposed to furnish the necessary equipment and fixtures to adequately equip the coffee shop and other concessions.

2. This lease shall be for the exclusive concessions limited to the area of the Administration Building and will include sale of food, drinks, refreshments, magazines, tobacco, novelties and other articles commonly sold or displayed at air line terminals, and the right to operate coin slot machines.

3. The period of this agreement shall be for ten (10) years with the option to renew on the same terms for an additional term of five (5) years.

4. Under the terms of our agreement dated August 1, 1942 with the City of Las Vegas for the use of McCarran Field, the City is obligated among other things to provide janitor service for the Administration Building; passenger, janitor and cleaning supplies as enumerated under Paragraph B below; and lighting and cooling as enumerated under Paragraph C below. In submitting this bid Western Air Lines, Inc. took into consideration that since it had employees at the airport twenty-four hours a day, it might be more satisfactory for all parties concerned if Western Air Lines, Inc. would relieve the City of this obligation and itself perform the duties and assume the expense as part of the agreement contemplated under this bid. The duties and expenses which Western Air Lines, Inc. would so assume and thereby relieve the City of Las Vegas are as follows:

A. Western Air Lines, Inc. will provide twenty-four hour per day inside janitor service for the term of this lease in the present building known as the Administration Building at McCarran Field.

B. Western Air Lines, Inc. will assume the cost of all replacement of light bulbs, sweeping compound, window cleaning fluid, soap, paper towels and toilet

2829

paper for the public rest rooms, furniture polish, floor wax and other miscellaneous janitor supplies. The above articles are to be supplied for the building known as the Administration Building at McCarran Field.

C. Western Air Lines, Inc. will assume the cost of the lighting and heating required in the present Administration Building, as well as operate and supervise the operation of the heating and cooling systems and generally supervise the Administration Building to insure its being well maintained and regulated.

5. Western Air Lines, Inc. agrees to furnish the City of Las Vegas with reports of the activities on the airport in conjunction with air transport passenger carrier operation (which should eliminate the need of the City of Las Vegas employing a Field Manager).

6. As consideration for the leasing to it of the above described premises and privileges, Western Air Lines, Inc. agrees to pay to the City of Las Vegas One Hundred Dollars (\$100.00) per month, payable at the end of each month during the period of the agreement.

7. It is understood that should the coffee shop be forced to discontinue operation or be removed from the airport known as McCarran Field, due to the war effort or by order of any government agency, that the rent for that period of no operation be canceled and a period of the same number of days be added to the lease at the end of the present lease at the same rental.

8. It is also understood that should gambling become illegal or the legal status of gambling change on the premises or if the Army orders gambling discontinued in the Administration Building at McCarran Field, that the rent for the concession be adjusted by mutual agreement of the City of Las Vegas and Western Air Lines, Inc., or if no agreement can be reached, that the rental shall be Fifty Dollars (\$50.00) per month.

9. The above rentals are in addition to those which the City will receive from Transcontinental and Western Air,

the Civil Aeronautics Authority and the United States Weather Bureau, who are now renters occupying space in the Administration Building at McCarran Field.

10. Western Air Lines, Inc. is exceedingly desirous of obtaining this concession in order that the standard of service may be maintained at the high level commensurated with that to which air line patrons are accustomed.

Respectfully submitted this seventeenth day of February, 1943.

WESTERN AIR LINES, INC.

By _____
Secretary

• • • • •

2878

Exhibit PC-12

165

| <u>Long Beach</u> | | | |
|-------------------|-------------------|-------------------|------------------------|
| <u>Canteen</u> | <u>Machines</u> | <u>Total</u> | <u>Grand Total</u> |
| | | | 15,571.71 |
|) (285.06) | - | (3,842.00) | 41,702.21 |
|) (728.65) | - | (4,138.86) | 57,408.00 |
|) <u>(707.42)</u> | <u>112.15</u> | <u>(3,830.10)</u> | <u>16,564.98</u> |
|) (1,721.13) | 112.15 | (11,810.96) | 131,246.90 |
| <u> </u> | <u> </u> | <u> </u> | <u> </u> |
|) (714.75) | 133.20 | (1,737.43) | 10,283.98 |
| <u> </u> | <u> </u> | <u> </u> | <u>(3,166.33)</u> |
|) (2,435.88) | 245.35 | (13,548.39) | 138,364.55 |
| <u> </u> | <u> </u> | <u> </u> | <u> </u> |

BLEED THROUGH- POOR COPY

2879A

Exhibit PC-14**ORIGINAL LEASE BETWEEN CITY OF LAS VEGAS
AND WESTERN**

THIS INDENTURE OF LEASE made this 1st day of August, 1942, by and between the CITY OF LAS VEGAS, a municipal Corporation, hereinafter called "Lessor," and WESTERN AIR EXPRESS CORPORATION, a Delaware corporation, hereinafter called "Lessee";

WITNESSETH:

WHEREAS, the Lessee is now, and for many years last past has been, engaged as a common carrier by air in the business of transporting passengers, property, and United States mail by airplane between the cities of Los Angeles in the State of California and of Salt Lake City in the State of Utah, via Las Vegas, Nevada; and

WHEREAS, said Lessee up until the date of this indenture has been the owner of the property hereinafter described; and

WHEREAS, said Lessee has this day conveyed all of the property hereinafter described to said Lessor in consideration of said Lessor granting to said Lessee a lease on said premises and certain operating rights, all as hereinafter more fully set forth;

Now, THEREFORE, in consideration of the premises and in consideration of the covenants and conditions herein contained, the parties hereto mutually agree as follows:

I.

Lessor does hereby demise, lease, and let unto Lessee, and Lessee does hereby hire and take from Lessor, the following premises and facilities, rights, licenses, and privileges in connection with and on the property and improvements of Lessor located near the City of Las Vegas, County of Clark, State of Nevada, and known as the Las Vegas Municipal

Airport, (which is more particularly described in Exhibit I hereto attached and made a part hereof), to wit:

A.

The use, in common with others authorized so to do, of said Airport and appurtenances, together with all facilities, improvements, equipment, and services which have been or may hereafter be provided at or in connection with said Airport from time to time, including, without limiting the generality thereof, the landing field and any extension thereof or addition thereto, runways, aprons, taxi-ways, sewerage and water facilities, flood lights, landing lights, control tower, signals, radio aids, and all other conveniences for flying, landings, and takeoffs of aircraft owned or operated by Lessee which use, without limiting the generality thereof, shall include:

2880 (1) The operation of a transportation system by aircraft for the carriage of persons, property, or mail, including charter and sight-seeing flights, (hereafter referred to as "air transportation").

(2) The repairing, maintaining, conditioning, servicing, parking, or storage of aircraft or other equipment.

(3) The training on the leased premises of personnel in the employ of or to be employed by Lessee and the testing of aircraft and other equipment; it being understood that such training and testing shall be incident to the operation by Lessee of its air transportation system.

(4) The sale, disposal, or exchange of Lessee's Aircraft, engines, accessories, gasoline, oil, greases, lubricants, and other equipment, or other fuel or supplies provided that the exclusive right of Lessee hereunder to sell gasoline, fuel, greases, and other lubricants upon said premises shall be limited to a period of fifteen (15) years from the date hereof, but the right to service by Lessee of Lessee's aircraft and of the aircraft operated by Lessee or belonging to or operated by a subsidiary or affiliated company of said Lessee shall continue during the life of this lease. Further-

more, such right shall include without limiting the generality thereof the right to install and maintain on said Airport adequate storage facilities for such gasoline, oil, greases, and other fuel or supplies either underground or on the surface, together with the necessary pipe, pumps, motors, filters, and other appurtenances incidental to the use thereof and the exclusive right to the use of the storage facilities now installed on said premises for such gasoline, oil, greases, and other fuel or supplies, together with the pipes, pumps, motors, filters, and other appurtenances connected therewith.

(5) The landing, taking-off, parking, loading, and unloading of aircraft or other equipment owned or operated by Lessee.

(6) The right to load and unload persons, property, and mail at said Airport by such motor cars, busses, trucks, or other means of conveyance as Lessee may choose or require in the operation of its air transportation system with the right to designate the particular carrier or carriers who shall or may transport Lessee's passengers and their baggage to and from the Airport.

(7) The right to install and operate advertising signs representing its business on the leased premises at Lessee's expense, the general type, design, and location of such signs to be subject to the approval of Lessor.

2881 (8) The right to install, maintain, and operate such radio communications, meterological, and aerial navigation equipment and facilities at Lessee's expense in, on, about, or near the premises herein leased on said Airport as may be necessary or convenient in the opinion of Lessee for its operations.

(9) The conduct of any other business or operations reasonably necessary to the proper conduct and operation by Lessee of an air transportation system for the carriage of persons, property, or mail by aircraft.

B.

The exclusive right for a period of ten (10) years from the date of this lease to sell to owners and operators of transient aircraft gasoline, oil, greases, lubricants, and other fuel; it being understood that the term "transient aircraft" shall not include aircraft owned by any person using said Airport as a home base; and it being further understood that the owners of aircraft using said Airport as a home base shall be permitted to supply and service their own equipment, gasoline, oil, greases, lubricants, and other fuel, if they so desire, but such owners shall not be permitted to sell to or service with gasoline, oil, greases, lubricants and other fuel the aircraft of others on said premises; and no vendor or supplier of gasoline, oil, greases, lubricants, or other fuel other than Lessee will be permitted to sell such products or service aircraft on or about said Airport during said period of ten (10) years.

It is further understood that after the expiration of said ten-year period and for the next ensuing five (5) years Lessee shall continue to have the exclusive right to sell gasoline, oil, greases, lubricants, and other fuel as in the preceding period provided; but Lessee agrees that during said period of five (5) years it will pay to Lessor the sum of two cents (2c) per gallon for each gallon of gasoline so sold to such transient aircraft, which payments shall not be added by Lessee to the sales price of gasoline sold by it; and in this connection Lessee agrees to furnish to Lessor on or before the 15th day of each month an accurate statement of the amount of gasoline so sold during the preceding calendar month, and at the same time will pay to the City the said sum of two cents (2c) for each gallon of gasoline sold as shown by said statement, provided that such sum shall not be applicable to gasoline used by Lessee in connection with its own operations.

C.

It is understood and agreed that Lessor reserves all other concessions at said Airport, including the sale of food and

beverages, notions, curios, magazines, newspapers, and periodicals, and slot machines.

2882

D.

Upon completion by Lessor of a hangar upon said Airport, Lessee shall have the exclusive use of sufficient space therein for housing and maintaining adequate facilities for normal and routine repairs and maintenance of its aircraft. In addition, Lessor shall make available to Lessee in said hangar, so long as unrented space shall be available and until Lessee shall construct at said Airport its own hangar or other suitable building, sufficient space for the storage of one airplane when required by Lessee. Lessor shall make available to Lessee adequate space for parking and storing not to exceed four (4) automobiles and for supplies used by Lessee in its operations, in said hangar or some other building erected by Lessor on said Airport and adapted for that purpose; provided, however, that Lessor shall not be required to furnish any such space if and when Lessee shall have constructed a hangar or other building at said Airport in which such facilities, airplane, automobiles and supplies may be respectively housed, maintained, parked and stored.

E.

Lessor shall make available to Lessee on said Airport adequate and sufficient space for the construction and installation of a hangar, shop, fuel tanks, and other buildings, equipment, and facilities deemed required by Lessee in connection with its operations, the location on said Airport of such hangar, shop, fuel tanks, and other buildings, equipment, and facilities to be subject to the approval of said Lessor.

F.

Lessee shall have the first choice of location and the exclusive use of not less than seven hundred fifty (750) square feet of space in the administration building on said Airport

for such uses as Lessee may desire to make thereof in connection with or incidental to its operations, such uses to include, without limiting the generality thereof, the sale of tickets, manifesting of passengers and cargo, handling of mail, baggage, and cargo, and the operation of general traffic, operations, and communications offices; provided, however, if the construction cost of said administration building exceeded or exceeds \$50,000.00, Lessee shall have the first choice of location and the exclusive use of not less than one thousand (1,000) square feet of space therein.

G.

The use by Lessee, its employees, passengers, guests, patrons, and invitees, in common with others, of all public space in said administration building and additional public spaces which may hereafter be made available in said administration building or any additions thereof, including, without limiting the generality thereof, the lobby, waiting rooms, hall ways, restrooms, and other public and
2883 passenger convenience.

H.

Lessee and its passengers, invitees, licensees, and employees shall have the use in common with other air transportation companies, of an adequate vehicular parking space located as near as possible to the administration building without charge to such passengers, invitees, licensees, or employees; it being understood that "passengers" as used in this paragraph includes persons calling for or delivering passengers.

I.

Lessee in common with other airlines shall have the right to erect, maintain, and operate poles, antenna, equipment, and facilities on and about said Airport as in Lessee's opinion may be necessary or convenient for Lessee's operation of remote control radio receiving and transmitting equipment, the location of said equipment and facilities on

or about said Airport shall be subject to the approval of Lessor. Lessor agrees to zone areas under its control surrounding Lessee's radio transmitting site to prevent the erection of poles, lines, power lines, buildings, and other structures which would prevent the proper operation of Lessee's radio and transmitting equipment.

J.

The full, unrestricted, and free access and ingress to and egress from the premises outlined in "A" to "I" inclusive, above, for Lessee, its employees, passengers, guests, patrons, invitees, suppliers of materials and furnishers of service, its or their aircraft, equipment, vehicles, machinery, and other property without charge to said employees, passengers, guests, patrons, invitees, suppliers of materials and furnishers of service, or their said property.

II.

Lessor acknowledges that the transfer from Lessee to Lessor of the real property on which said Airport is located constitutes full consideration for this lease; and agrees that during the term hereof Lessee shall not be obligated or required to pay any rents, tolls, charges, or license fees to Lessor, except as herein otherwise expressly provided.

III.

Subject to earlier termination, as hereinafter provided, the term of this lease shall be for thirty (30) years from and after the date hereof.

IV.

Lessor represents that it has the right to lease said Airport, together with all of the facilities, rights, licenses, and privileges herein granted, and has full authority and
2884 power to enter into this lease in respect thereof.

V.

Lessee shall have the full right of purchasing at said Airport or elsewhere gasoline, oil, fuel, lubricating oil, grease,

or any other materials, equipment, or supplies and aircraft from any person, or company of its choice, and no charges, fees, or tolls of any kind shall be charged by Lessor, directly or indirectly, against Lessee or its suppliers for the privilege of using, storing, withdrawing, handling, consuming or transporting the same to, from, or on said Airport. Nothing in this paragraph contained shall be construed as affecting the right of Lessor to keep in force all ordinances in effect on November 1, 1940 imposing license fees on persons, firms, and corporations doing business in the City of Las Vegas, or similar ordinances.

VI.

Lessor agrees that no charges, fees, tolls, licenses, taxes, or assessments, other than herein expressly provided for, shall be charged or collected by it, directly or indirectly, from Lessee or any other persons, including, without limitation, taxi and limousine companies or operators, employees, suppliers of materials, or furnishers of service for the privilege of serving Lessee or transporting, loading, unloading or handling persons, property, or mail to, from, into, or on said Airport in connection with Lessee's business; provided, however, that Lessor shall not be prevented from imposing upon and charging taxi and limousine companies or operators serving said Airport the same City license fee imposed upon and charged all taxicabs or taxicab companies alike doing business in the City of Las Vegas. Nothing in this paragraph contained shall be construed as affecting the right of Lessor to keep in force all ordinances in effect on November 1, 1940 imposing license fees on persons, firms, and corporations doing business in the City of Las Vegas, or similar ordinances.

VIII.

If Lessee is required to procure any licenses or permits from the authorities of the City of Las Vegas to authorize and permit it to carry on any of the activities and operations

which Lessee is authorized or permitted to carry on under this lease, Lessee may deduct the cost of such licenses and permits other than those imposed by ordinance in force at the execution of this lease from any rentals or fees payable by it hereunder, and if Lessee is required to procure any such licenses or permits from the County of Clark or the State of Nevada, Lessee may deduct from any rentals or fees payable by it hereunder the portion, if any, of the cost of such licenses or permits remitted by law or regulation to the City of Las Vegas or remitted for use in connection with the construction, improvement, maintenance, or operation of said Airport.

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VIII.

Lessor agrees that the runways on said Airport and the field lighting equipment now or hereafter constructed thereon, and all appurtenances, equipment, facilities, and services of and at said Airport, shall at all times be maintained by and at the expense of Lessor and in such condition and up to such standard as may be required by the Civil Aeronautics Board for the operation of aircraft now or hereafter operated by Lessee in the conduct of its operations; and Lessor further agrees that all buildings belonging to Lessor and now or hereafter constructed on said premises shall be kept in a reasonable state of repair by and at the expense of Lessor.

Lessor agrees to keep said Airport free from obstructions for the safe, convenient, proper, and continuous use thereof by Lessee, and to maintain and operate said Airport in all respects at least equal to the highest standards of ratings for airports of similar size and character issued by the Civil Aeronautics Board and in accordance with all of the rules and regulations of the Civil Aeronautics Board.

It is expressly understood that Lessor will keep the public space in the administration building attractively furnished, and will provide and supply heat, light, electricity, cooling, and water for the public space and Lessee's exclusive space

in the administration building; janitors or other cleaners necessary to keep the Airport and the said spaces in the administration building at all times clean, neat, orderly, sanitary, and presentable; all attendants necessary to facilitate the use of the Airport and the administration building and the appurtenances, facilities, and services as aforesaid by anyone hereunder entitled to use the same, and will also furnish the necessary electrical energy for the operation of all field lights, it being understood that the cost of power and electricity for the operation of Lessee's radio equipment, fuel distribution equipment, air compressors, other ground equipment, and for charging batteries of Lessee shall be borne by Lessee. It is further understood that Lessee shall pay for its own exclusive telephone service.

IX.

Lessor covenants and agrees to make available reasonable and adequate space and proper facilities in the administration building for the use of the United States Customs and Immigration authorities, representatives of the United States Health Department, the United States Department of Agriculture, the Civil Aeronautics Board, and the United States Post Office Department upon such terms and conditions as may be acceptable to said agencies.

X.

Lessee may, at its own cost and expense, erect on or install on said airport in convenient spaces to be approved by the City any buildings or structures, including storage tanks or equipment above, on or under ground that it shall determine to be necessary or convenient for use in connection with its operations. Any such buildings erected shall be designed so as to harmonize with the other buildings adjacent thereto. No restrictions shall be placed upon Lessee as to the architects, builders, or contractors who shall be employed by it in connection with the erection of any such buildings, and Lessor shall provide free ingress

and egress to and from said spaces for any person or material or thing connected with the erection of any such buildings or structures.

Any buildings, hangars, structures, fixtures, and equipment heretofore or hereafter erected or installed by Lessee are to remain the property of Lessee during the term of this lease or any renewal thereof. All of said buildings, hangars, structures, fixtures, and equipment hereinabove referred to may be removed by Lessee at any time up to six (6) months after the termination of this lease, and if not so removed, shall become a part of the land on which they are erected, and title shall thereafter vest in the name of Lessor.

XI.

Lessee agrees to furnish sufficient personnel for the reasonable servicing of transient aircraft at said Airport with gasoline, oil, grease, fuel, and other lubricants and for the operation of its fuel storage plant and equipment.

XII.

It is understood and agreed that if the requirements of Lessee are such that additional space in said administration building or any addition thereto is needed by Lessee, and if such space is not already used by other paying tenants of Lessor, then and in such event Lessee shall have the right to use such necessary additional space; provided, however, in the event Lessee shall be placed in possession of additional space in the administration building under this paragraph and thereafter Lessor receives an acceptable and bona fide offer from a prospective tenant to rent such space on a revenue basis, Lessee shall have the option of disposing such space or remaining in possession upon payment of the same revenue offered by the prospective tenant and for the same term embraced in the offer.

XIII.

Lessor shall adopt and enforce rules and regulations which Lessee agrees to observe and obey with respect to the use of the Airport, which shall provide for the safety of those using the same; provided that such rules and regulations shall be consistent with safety and with rules, regulations, and orders of the Civil Aeronautics Board with respect to aircraft operations at said Airport; and provided further that such rules and regulations shall not be inconsistent with the provisions of this lease or the
2887 procedures prescribed or approved from time to time by the Civil Aeronautics Board with respect to landing and taking-off of Lessee's aircraft at said Airport.

XIV.

Lessor shall have no control whatsoever over the rates, fares, or charges that Lessee may prescribe for any of its services by air or land to, from, or through said Airport, or between the Airport and its ticket offices or other stopping places in the City of Las Vegas, the intent hereof being that Lessee may establish such rates, fares, and charges as it, in its uncontrolled discretion, may desire to establish, subject, however, to any, and all appropriate rules, regulations, or orders of the Civil Aeronautics Board.

XV.

If the administration building shall be damaged by fire or other casualty, the same shall be repaired with due diligence by Lessor at its own cost and expense. In case said administration building is completely destroyed by fire or casualty, or so damaged that it cannot reasonably be repaired within thirty (30) working days, then and in such event Lessee shall have the right to construct at a convenient place upon said Airport a temporary building for the exclusive use of said Lessee, its employees, patrons, passengers and invitees. It is understood and agreed that Lessor shall keep the administration building insured

against fire, earthquake, and elements at its highest insurable amount, and will pay the premiums on such insurance; and it is agreed that in case of loss under any such policy that the amount recovered from such insurance companies shall be used exclusively in the repair and reconstruction of the premises so damaged. It is further understood and agreed that Lessor will also insure and keep insured any other building erected upon said premises by Lessor, and that the proceeds derived from any loss under such policy shall be used in repairing or replacing the property so damaged.

XVI.

In the event Lessee shall abandon and discontinue the conduct and operation of, or be permanently prevented by any final action of any Federal or State authority from, conducting and operating its air transportation system at the Airport, or in case Lessee shall fail to perform, keep, and observe any of the terms, covenants, or conditions herein contained on the part of Lessee to be performed, kept, or observed, Lessor may give Lessee written notice to correct such condition or cure such default, and if any such condition or default shall continue for sixty (60) days after the receipt of such notice by Lessee, then Lessor may, after a lapse of said sixty (60) days period, and prior to the correction or curing of such condition or default, terminate this lease by a thirty (30) days written notice; and the term hereby demised shall thereupon cease and expire at the end of such thirty (30) days in the same manner and to
 2888 the same effect as if it were the expiration of the original term.

XVII.

Lessor agrees that upon the performance of the conditions, covenants, and agreements on the part of Lessee to be performed hereunder Lessee shall peaceably have and enjoy the leased premises and all the rights and privileges

at said Airport, its appurtenances and facilities herein granted.

XVIII.

Whenever the term "Civil Aeronautics Board" is used in this lease it shall be construed as referring to the Civil Aeronautics Board created by the Federal Government under the Civil Aeronautics Act of 1938, or to such other Federal Government authority which may be the successor thereto or be vested with the same or similar authority.

XIX.

Notice to Lessor provided for herein may be served by mailing the same by registered mail, postage prepaid, addressed to the City Clerk of the City of Las Vegas, Las Vegas, Nevada; and notice to Lessee may be served by mailing the same by registered mail, postage prepaid, addressed to Lessee at Burbank, California.

XX.

All the covenants, stipulations, and agreements in this lease shall extend to and bind the successors and assigns of the respective parties hereto.

XXI.

This lease shall be deemed to be made in and construed in accordance with the laws of the State of Nevada.

IN WITNESS WHEREOF, the City of Las Vegas, a municipal corporation, has caused this lease to be executed in duplicate by its Mayor and attested by its City Clerk under the seal of said City, and said Western Air Express Corporation has caused this lease to be executed in duplicate in its corporate name by its President, or one of its Vice Presidents, and its corporate seal to be hereunto affixed and attested by

2889 its Secretary, or one of its Assistant Secretaries, as of the day and year first above written.

THE CITY OF LAS VEGAS
By /s/ JOHN L. RUSSELL
Its Mayor

Lessor

WESTERN AIR EXPRESS CORPORATION
By s/s CHARLIE N. JAMES
Its Vice President

Lessee

Attest:

Viola Burns
City Clerk

Attest:

Paul E. Sullivan
Secretary

STATE OF CALIFORNIA, }
County of Los Angeles } ss:

On this 4th day of September, A. D., one thousand nine hundred and 42, personally appeared before me, Earnest H. Brown, a Notary Public in and for the County of Los Angeles, State of California, Charlie N. James, known to me to be the Vice President of the Corporation that executed the foregoing instrument, and upon oath did depose that he is the officer of said corporation as above designated; that he is acquainted with the seal of said corporation, and that the seal affixed to said instrument is the corporate seal of said corporation; that the signatures to said instrument were made by the officers of said corporation as indicated after said signatures, and that the said corporation executed the said instrument freely and voluntarily and for the uses and purposes therein mentioned.

IN WITNESS WHEREOF, I have hereunto set my hand and
affixed my Official Seal, the day and year in this certificate
first above written.

/s/ EARNEST H. BROWN

Notary Public in and for the
County of.....
State of Nevada.

My Commission expires Dec. 5th, 1944.

• • • • •

Serial Number E-4870

Served: Nov. 27, 1950

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UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 et al.

WESTERN AIR LINES, INC.

AND

INLAND AIR LINES, INC.

MAIL RATES

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith.

Opinion

Decided: November 24, 1950

The proper date from which to determine a carrier's mail rate, when it has challenged the adequacy of its rate by the filing of a petition, is the date of petition.

Whether a carrier has gains or losses after it files a rate petition cannot be the determinant of when the review period commences.

The "all other revenue" clause of Section 406(b) requires that net revenues available to a carrier from sources other than regular air transport operations be used to reduce its need for mail pay, unless the carrier clearly establishes that the revenue producing activity is entirely separate and apart from its air carrier activities.

Revenues from restaurants and cafes, canteens, and coin-vending and slot machines should be included in the determination of Western's mail pay need.

Net profit of \$1,099,000 from the sale of Route 68, with terminals at Los Angeles and Denver, is "other revenue"

within the meaning of Section 406(b) of the Act, and Western's mail pay need should be reduced accordingly.

3492 The use of costs adjusted by the Board in other proceedings in cost comparisons for the purpose of determining amounts of excess expense is an essential part of the rate-making process.

The application of the direct labor dollar basis of allocating indirect maintenance expense to equipment types is warranted and proper.

The most appropriate single basis of comparison for the purpose of determining the extent to which a carrier's general and administrative expense is excessive found to be the ratio of such expense to all other cash operating expenses.

Costs arising from the development, operation, and divestment of a substantial portion of a carrier's route system are a proper offset against profits realized by the carrier as a result of the disposal of the route.

The public interest requires that mail pay not be burdened by depreciation charges on aircraft that are not used and useful for the operations performed.

Provision for Federal income taxes should be based on constructive profit reduced by expenses which will never be recognized for mail rate purposes but which are considered properly deductible for tax purposes.

The fair and reasonable compensation for the transportation of mail by aircraft for the entire past period for Western is \$3,580,526, and for Inland, \$1,022,793, and, accordingly, there has been an overpayment of temporary mail pay of \$671,474 and \$76,207, for Western and Inland, respectively.

Appearances:

D. P. Renda for Western Air Lines, Inc., and Inland Air Lines, Inc. *Frank J. Delany, Frederick E. Batrus, and Eugene H. Brahm* for Post Office Department

Harry H. Schneider, Public Counsel

OPINION

BY THE BOARD:

This is a consolidated proceeding for determination, pursuant to Section 406 of the Act, of rates of mail compensation of Western Air Lines, Inc. (Western) and its subsidiary Inland Air Lines, Inc. (Inland) for periods prior 3493 to January 1, 1949. The proceeding was initiated by a mail rate petition filed by Western on April 26, 1944, in Docket No. 1374, which was later consolidated for disposition with the petition of Inland in Docket No. 2870.

In response to the petitions, on December 30, 1948, we issued Statements of Tentative Findings and Conclusions proposing specified mail rates for each carrier and accompanying Orders to Show Cause why such rates should not be finalized (Orders Serial Nos. E-2333 and E-2334). Separate rates were provided Western for the past period, May, 1944, through December 31, 1948,¹ and for the future period begun January 1, 1949. This also obtained as regards Inland, the past period in its case running from March 28, 1947, through December 31, 1948.

The rates proposed for the future were uncontested and were finalized on May 6, 1949 (Orders Serial Nos. E-2795 and 2796). Objection was raised, however, by Western and the Postmaster General² to various of our tentative findings and conclusions pertaining to the past periods. In accordance with the Procedural Regulations the issues arising out of the various objections were defined, hearing held thereon, and briefs and oral argument presented to the Board.

3494 The proceeding is now ready for our decision of those issues.³ As regards all other matters entering into

¹ Although Western's petition was filed April 26, 1944, our Show Cause Order proposed that May 1, 1944, be deemed the filing date for rate purposes, and this proposal has been accepted without question by all parties.

² Formal intervention was granted the Postmaster General upon petition by Order Serial No. E-2917, June 7, 1949.

³ With the exception of the Federal income tax issue, dealt with *infra* at pp. 48-50, all of the issues concern Western alone. Since Inland's mail pay is determined largely on the basis of allocations of expenses to and from Western, however, to the extent that any issue before us pertaining to Western is the subject of allocation, our decision thereon affects Inland's requirements and has been reflected in the mail rate fixed herein for Inland.

the determination of mail rates for each of the two carriers, our findings in the Tentative Statements are uncontested, so that the resolution of the issues before us will produce the fair and reasonable final mail rates, which will replace the temporary rates previously established for the respective past periods.⁴

Period For Which Rate Will be Fixed for Western

One of the most important questions before us is whether the rate period for Western shall commence as of the date of filing of its petition, May 1, 1944, or as of some other date, Western's contention being January 1, 1946. We discussed this matter in the Tentative Statement and found that the proper period for the determination of Western's mail rate was from the date of petition to December 31, 1948. Also our temporary rate order of February 1949, was issued at Western's request for the period May 1, 1944, through December 31, 1948. Western contends, however, that the Board has the power under the Act to move from the date of petition to January 1, 1946, and that precedent warrants the exercise of its discretion in doing so here.

The underlying reason for Western's position is that the mail pay it received under the challenged 60 cent ton-mile rate of November 1, 1943, resulted in highly profitable operations from May 1, 1944, through December 1945, 3495 after which substantial losses were incurred. Thus, if we eliminated the portion of the rate period prior to January 1, 1946, Western would receive approximately \$885,000 more mail pay than if its operations were reviewed from the petition date.

The adoption of Western's contention would be contrary to our views of the Board's responsibility under Section 406, which empowers the Board

* * * to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facil-

⁴ Temporary rate Orders Serial Nos. E-2506, 2507, and 2531.

ities used and useful therefor, and the services connected therewith, * * * and to make such rates effective from such date as it shall determine to be proper.

We construed this section in the *TWA* case⁵ before the Supreme Court to mean that our mail rate order can be effective no earlier than the date a proceeding is initiated by the filing of a carrier's petition challenging its mail rate. This construction was promised upon the fact that the Act was patterned after conventional public utility rate-making statutes, which embody the concept of establishing rates for the future, rather than on a cost-plus basis. We declared that the effect of our mail rate policy would be to discourage the filing of protective petitions by carriers seeking to guarantee to themselves a cost-plus basis of mail payment, since our order in any mail rate case would be effective as of the filing date of the carriers' petition, and any profits earned thereafter in excess of a fair and reasonable return on investment would result in a reduction of the rate from the date of petition.

3496 Whether a carrier has gains or losses after it files a rate petition cannot be the determinant of when the review period commences. What Western contends for here is a better than cost-plus basis of rate-making, since it seeks to retain all of its earnings during the profitable period of operation (May 1, 1944-December 31, 1945), while at the same time it calls on the Government to make up all losses from the beginning of the period in which they were incurred. It would, of course, be unfair to the Government to expect it to make up losses incurred after the petition but to permit the carriers to retain any profits. But there are broader considerations of statutory construction and rate-making policy which weigh heavier in our decision. Our failure to review a carrier's operations from the petition date in circumstances such as are present here would be understood by all need carriers as meaning that we would

⁵ *Transcontinental & Western Air, Inc., v. Civil Aeronautics Board*, 169 F. (2d) 893, *affirmed* 336 U.S. 601 (1949).

not disturb profits earned in excess of a fair and reasonable return on investment after the filing of a petition, but would only reimburse a carrier for any losses that might eventuate. In addition, realizing the obvious advantage of such a policy, need carriers would be encouraged to maintain protective petitions on file, as insurance against the possibility of unexpected losses. The large number of petitions that would be continuously on file would create an administrative burden of serious proportions. More important, however, they would nullify our efforts to place carriers on prospective future rates which will remain final for a reasonable period.

We have previously set forth the importance of prospective rate-making as follows (*PCA et al, Motions*, 8 C.A.B. 685, 696 (1947)) :

The respondents in effect urge a cost-plus subsidy plan, in place of a traditional prospective rate-making technique. Under the latter plan there is a twofold pressure to economy and efficiency caused by the necessity of living within a known rate and by the prospect of being able to retain earnings which may be effected under the rate. Administration of the mail pay provisions of the Act through the instrumentality of a prospective rate is designed to foster a sound air transport system in the interest of the traveling public, the post office, and the national defense while retaining in this industry competitive characteristics which, under our economy, are deemed desirable and productive of public benefit.

This interpretation of the Act was sustained by the courts.⁶ Any interpretation which holds that a carrier can enjoy the protection against loss under the Act and at the same time reap the benefits of all gains during the period when a petition is on file is irreconcilable with the provisions and the intent of the Act.

Our decisions in recent cases have been consistent with

⁶ *Transcontinental & Western Air, Inc., v. Civil Aeronautics Board*, 169 F. (2d), 893, *affirmed* 336 U.S. 601 (1949).

this interpretation of our responsibility for reviewing a carrier's operations from the date of petition, where a carrier has challenged the adequacy of its rate, particularly in the mail rate cases of Braniff Airways and Continental Air Lines.⁷ In the *Braniff* case the carrier challenged its final rate by filing a petition only two months after such rate had been fixed and later sought to withdraw its petition for an increased rate. This was denied on the grounds that we were required to determine whether Braniff had earned in excess of a fair and reasonable return, which would necessitate reduction of its rate from the date of petition. It was only after we found that Braniff had not earned an unreasonable return that we re-established the challenged rate for the entire period. In the *Continental* case, the carrier's earnings during the first part of the rate period under the challenged rate were excessive, whereas in the latter part of the period the carrier required additional mail pay. The mail rate was fixed for the entire period and, consequently, the excess earnings were offset against the need. Had we followed Western's views, we would have excluded the profitable portion and fixed a rate only for the period when losses were incurred.

Western relies heavily on the precedent it claims was established in the *Panagra* case⁸ and the *Chicago & Southern* case⁹ as supporting its claim for the exclusion of the years 1944-1945 from the rate period. There were important distinguishing factors, however, between the *Panagra* case and the situation here. Although we found that Panagra had received mail payments in excess of a fair and reasonable return on investment, we determined that a reduction in mail pay was not justified because of the uncertainties of wartime operations as well as the requirements for operating its international routes, and our final order in that case

⁷ Braniff Airways, Inc., Mail Rates, Docket No. 3601, Order Serial No. E-4285 (June 5, 1950; Continental Air Lines, Inc., Mail Rates, Docket No. 3281, Order Serial No. E-4332 (June 21, 1950).

⁸ Panagra, Mail Rates, 3 C.A.B. 550 (1942).

⁹ Chicago & Southern Air Lines, Inc., Mail Rates, 9 C.A.B. 786 (1948).

left the challenged rate unchanged for the entire period. In this proceeding, however, we have increased the rate for the entire period. Moreover, the uncertainties facing Panagra in its wartime operations are not present in the case of Western. The other wartime cases cited by Western where we refused to reduce mail pay earned under a challenged rate fall into the same category as Panagra. In the *Chicago & Southern* case we decided that the earnings in the early part of the rate period were not in excess of a fair and reasonable return and that we were, therefore, not required to review its operations back to the petition date. In this case we have subjected the entire period back to the petition date to closer scrutiny than we did in the case of Chicago and Southern, and to that extent our decision here goes further

than did the *Chicago & Southern* case. In any event, 3499 to the extent that our decisions in the Chicago &

Southern and earlier cases are inconsistent with the principle applied here as well as in the Braniff and Continental cases, the earlier cases are overruled.

One of Western's contentions is that the inclusion of the twenty months of 1944-1945 in the rate period will result in a recapture of its earnings under the then existing rate. In this connection, it claims that the resulting mail rate in the early portion of the rate period does not satisfy the Constitutional requirements for reasonable compensation for the transportation of mail. The mail rate we have provided for the entire period, equivalent to 99.4 cents per mail ton-mile, is higher, however, than the rate challenged in Western's petition, and satisfies Western's break-even need plus a fair return on investment. It is apparent, therefore, that there has been no recapture of mail pay, and that the issue of constitutional adequacy of the mail rate as determined for the review period has no merit. Although it is obvious that while any given mail rate might be inadequate for a selected portion of the whole period, this is not a proper

test of the adequacy of mail rates, and it has been consistently so held.¹⁰

Western also claims that we do not have the authority to reduce its rate in the years 1944-1945, since its petition was limited in scope to an increase in the challenged rate. Although we do not believe that the terms of a petition are controlling in determining a fair and reasonable mail rate, nevertheless, as we pointed out above, Western is receiving an increase in its rate for the entire period, and, consequently, we can attach no validity to the claim that the rate may be lower for a portion of that period. By filing its petition on May 1, 1944, Western indicated that it was a

3500 need carrier, and desired that its rate be revised from that date forward. It had no reason to expect that a rate would be established other than in accordance with its need. *Cf. Tagg Bros. & Moorehead v. United States*, 280 U.S. 420.

As a result of the foregoing, we find that the proper period for the determination of the mail rate for Western in the instant proceeding is from May 1, 1944, through December 31, 1948.

Restaurant and Concession Revenues

This proceeding presents two issues relating to the question of what properly may be considered "other revenue" in determining need for mail pay arising from (1) revenues from the operation by Western of restaurants and cafes, canteens, and coin-vending and slot machines at Salt Lake City, Utah, Las Vegas, Nevada, and Long Beach, California, and (2) the net profit from the sale of Route 68 to United Air Lines, Inc.

Considering first the restaurant and concession revenues, Western claims that (1) these operations were not a part of its common carrier activities, (2) they were segregated

¹⁰ *Panagra, Mail Rates*, 3 C.A.B. 550 561-2 (1942); *Braniff Airways, Inc. Mail Rates*, 3 C.A.B. 633, 637 (1942); *Delta Air Lines, Inc., Mail Rates*, 9 C.A.B. 645 (1948); *American Airlines, Inc., Mail Rates*, 6 C.A.B. 567 (1945); *City of Knoxville v. Knoxville Water Co.* 212 U.S. 1 (1919).

from those activities, and (3) the Act did not intend that revenues from other than air carrier functions be included in determining need. Western reported net revenues from these activities during the rate period in the amount of \$128,081, which it agrees should be reduced to approximately \$88,000 in order to reflect the offset of certain expenses applicable to the concession operations charged to operating expenses.¹¹ We shall assume this amount to be the net revenues for the purpose of our consideration here, although the record suggests, as pointed out by Public Counsel, that the amount would be lower had Western been able to segregate or allocate additional expenses related to these various activities.

Section 406(b) of the Act requires the Board in determining mail pay to consider :

* * * The need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

In our previous interpretation of this language we have not considered revenue from all sources as available to reduce the carrier's need. The controlling consideration has been the relationship of the revenue producing activity to the operations of the air carrier under its certificate of public convenience and necessity. Typical of activities where the revenue was considered in reducing "need" in previous Board cases are the sale of gas and oil, rents of buildings and other properties and other similar incidental items, the sale of aircraft which had never been placed in service

¹¹ The Uniform System of Accounts for Air Carriers requires that incidental revenues be reported as the net amount after all direct costs.

as well as aircraft and equipment which had been used in the operations, and charter operations.¹² In those cases where we have excluded "other revenue" in determining need there has been a clear indication that the activity in question was completely divorced from the air carrier functions and could have been conducted without the existence of a certificate of public convenience and necessity. Included in this category were the operation of a private school for pilot training and crop dusting activities and profits from investment in a foreign subsidiary.¹³

The controlling consideration, in our opinion, is whether the revenue generally derives its being from the operation of the air carrier under its certificate of public convenience and necessity. Where the activity from which the income arose is related to the air carrier functions, such income should be considered as "other revenue." In view of the broad statutory language referring to *all* other revenues and the desirability of reducing government support where the carrier has net income available to it from other sources to support its certificated operations, we will conclude that such revenue should be used to reduce need unless the carrier clearly establishes that the revenue producing activity is entirely separate and apart from its air carrier activities.

Under this test it is clear we should consider the restaurant and concession revenues as reducing Western's need. It appears from the record that the operations in question were in fact incidental to Western's common carrier activities. They were financed out of Western's work-

¹² Charter operations, *Pan American Airways, Inc., Pacific Mail Rates*, decided August 31, 1942, Docket No. 300, p. 13; profit arising from the sale of aircraft, *Colonial Airlines, Inc., Mail Rates*, 4 C.A.B. 71 (1942); *TWA, Mail Rates*, 4 C.A.B. 139 (1943), *Chicago & Southern A.L., Mail Rates*, 3 C.A.B. 161 (1941); even before placed in operation, *Pan American Airways Co. (Nov.) Mail Rates*, decided August 31, 1942, Docket No. 300, p. 11; sales of gas and oil, *TWA, Mail Rates*, 2 C.A.B. 226, 236 (1940).

¹³ Private training schools, *Northeast Airlines, Inc., Mail Rates*, 4 C.A.B. 181, 185 (1943), and *United Airlines, Inc., Mail Rates*, 1 C.A.A. 752, 764 (1940); crop dusting activities, *Delta Air Lines, Inc., Mail Rates*, 3 C.A.B. 261 (1942); *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C.A.B. 267 (1947).

ing capital and utilized other assets and facilities which were common to the regular air transportation services and which were included in the investment base upon which we have provided a return. The operations were supervised by Western's executives, and various accounting, personnel, and legal functions were performed by employees of the air carrier, the expenses of which are inseparable from those charged for normal operating expenses. The various concessions were operated for the convenience of airline passengers and employees and airport visitors. Western operated its own in-flight kitchen at Salt Lake City, and therefore, the operation of the restaurant, the only one of the three that made a profit, was integrated with Western's normal airline operations.¹⁴ Furthermore, although the record shows that Western obtained the restaurant and slot machine concession at the Las Vegas airport by bid, the fact that it had obtained a lease for its air transport operations and the concession for the exclusive sale of gas and oil in consideration for the transfer to the city of the land on which the airport is located, plus the fact that it conducted commercial airline operations at the airport, was undoubtedly given some weight in the selection of Western to operate the other concessions. The close tie-in with the air carrier operations of Western seems to have been recognized when the leases were drawn, and a clause was inserted giving Western the right to terminate the lease if commercial operations were suspended at the airport. Nor is it inappropriate to consider that the same lease provided for the sale of gas and oil at the airport, and

¹⁴ Western argues that our decision in *Chicago & Southern Air Lines, Inc., Mail Rates*, 3 C.A.B. 181 (1941), where we excluded the estimated loss from operation of a cafeteria in determining need, implies that revenues from this type of operation will also be excluded. The question as to whether the loss would be underwritten with mail pay is not controlling in determining whether the revenue should be considered as reducing mail pay. Quite apart, however, from this consideration, Western misconstrues the holding in the *Chicago & Southern* case. In that case the Board was estimating expenses for a future period. We merely stated that we saw no reason why the cafeteria should operate at a loss in the future. We did not rule on whether an actual loss from the cafeteria incurred under honest, economical and efficient management would have been met.

that the profits from these sales were reported in incidental revenues, which were taken into account in determining need. Western has not questioned our including these revenues from an activity which appears to be no different in nature from the sale of food and the operation of the canteen and coin machines at Las Vegas.

The real test, then, in the application of the "other revenue" clause of the Act lies in the extent to which a showing can be made that any revenue producing activity of the air carrier is a separate and distinct operation apart from the air transportation services performed. That showing has not been made here, and we have, therefore, included the restaurant and concession revenues in determining Western's mail pay need. If in future mail rate cases circumstances disclose that revenues are derived from unrelated activities of an air carrier, their exclusion may be warranted, but the mandate of the Act for underwriting the operations of need carriers includes the corollary consideration that all revenues generated by the air carrier be used first to reduce the contribution of the Government, unless compelling reasons dictate otherwise. The rights that are granted under a certificate of public convenience and necessity carry with them the obligation of management to exercise its initiative in developing the maximum attainable revenues from the operation of its air transportation services and activities incidental thereto.

3505

Profit from the Sale of Route 68

The second "other revenue" issue and the most important issue dollar-wise in this proceeding is whether the profit realized by Western from the sale to United Air Lines, Inc., of Route No. 68, extending from Los Angeles to Denver, together with the air carrier property related thereto should be considered in determining its need for mail pay. It is clear that to the extent that there was a profit, Western's need for mail pay support was reduced accordingly. There is no requirement under the Act that we dupli-

cate this revenue with mail pay unless we find a controlling practical reason for doing so, such as being unrelated to air carrier activities as discussed above, or unless the results of our decision would thwart the objectives of the Act for the development of air transportation. As we shall discuss below, there do not appear to be any compelling considerations here that would justify the exclusion of this profit in determining Western's need.

The sale of Route 68 was approved by the Board on August 25, 1947, in the *United-Western, Acquisition Air Carrier Property* case (8 C.A.B. 268) for the sum of \$3,750,000, and the transaction was consummated on September 15, 1947. In that decision we were not concerned with the issue of the treatment of any profit realized by Western in relation to its need for mail pay. Our approval was directed solely toward whether the transfer of the route and the price to be paid were in the public interest and toward the investment value for rate-making purposes of the properties acquired by the purchasing carrier.

Western transferred operating property and equipment to United consisting of four DC-4 aircraft, various spare parts and equipment, ground and station equipment, and miscellaneous supplies, having a book value of \$1,350,652,000 at the time of sale. After charges of approximately \$98,000, representing the cost of cancelling DC-6 purchase commitments and miscellaneous expenses connected with the sale, Western reported a book profit on the transaction of \$2,124,000. There were certain other costs, however, which Western incurred as the result of the development, operation, and divestment of Route 68, and those should be considered in determining the amount of the real profit whose treatment is at issue here. As discussed in a later section of this opinion, we have determined that the amount of \$1,025,000 of extraordinary costs should be properly offset against the profit of \$2,124,000, resulting in a "net" profit to Western of \$1,099,000 from the sale of the route.

In all of our decisions where a carrier has realized a profit from the sale or retirement of operating property of the air carrier, we have consistently regarded such gains, after offset of any losses, as "other revenue" in determining need.¹⁵ In this very proceeding we have offset a profit of \$155,000 from the sale of DC-3 and DC-4 aircraft, which was the excess after deduction of losses from other retirements, against Western's need, and our power or discretion in so doing has never been questioned by Western throughout this proceeding. There can be no doubt that the transfer of Route 68 and equipment used in its operation involved air carrier property by every possible construction of the term. The route certificate and the equipment made possible the operation of air transportation services and were an integral part of Western as an air carrier. The large amount of the profit or the fact that the transaction consisted of elements of tangible and intangible property does not change the nature of the transaction nor affect the treatment of the revenues from the sale.

3507 We indicated in the *Route 68 Acquisition* case, *supra*, that the fair market value of the tangible property was \$2,250,000. After the deduction of the book value of \$1,528,000 at September 15, 1947, the profit on the tangible property becomes \$722,000. Consequently, the remaining portion of the \$1,099,000 net profit for the route sale may be considered to apply to the intangible elements of the sale. Nevertheless, the tangible and intangible elements go together to make up the one transaction, and we cannot consider the profit from the intangibles any less valid a source of other revenue than that attached to the tangible property. Both were realized by virtue of benefits accruing to Western from its certificate of public convenience and necessity, which it received from the Government. While this same certificate also entitled the carrier to subsidy mail pay to

¹⁵ Colonial Airlines, Inc., Mail Rates, 4 C.A.B. 719 (1942); TWA, Mail Rates, 4 C.A.B. 139 (1943); Chicago & Southern Air Lines, Inc., Mail Rates, 3 C.A.B. 161 (1941); Continental Air Lines, Inc., Mail Rates Docket No. 3281, Order Serial No. E-4332 (June 21, 1950).

cover its need for revenue under honest, economical, and efficient management, it would be contrary to the public interest to use public funds to subsidize a need which had already been covered by profits accruing from benefits under the certificate. Cf. *Inland Air Lines, Inc., Mail Rates*, 1 C.A.A. 155, and *Pan American Airways, Inc., v. Civil Aeronautics Board*, 171 F. (2d) 139 (App. D. C. 1948). This in no sense curtails the carrier's rights under the certificate, among which is the right to receive subsidy mail pay based upon need, but merely offsets against these rights all special benefits in the form of profits realized by virtue of having been awarded the certificate. In the absence of subsidy need the full profit from the sale of Route 68 would have accrued to the benefit of the carrier.

Western's principal contention is that inclusion of the profit from the Route 68 sale as "other revenue" would adversely affect the incentive for air carriers to accomplish necessary route adjustments through voluntary route trans-

ferts and mergers or consolidations. We cannot accept the hypothesis, however, that readjustment of

the route pattern must be conditioned on the realization of profits by need carriers from such transactions, which they will be allowed to retain regardless of need, nor will our decision of this issue deter voluntary adjustments that are justified by long range economic considerations. The incentive of a carrier wishing to dispose of a route or to merge is to correct a situation which is inimical to its best interests, such as the operation of an uneconomical route that will mitigate against its over reaching self-sufficiency. The incentive to divest itself of such a route should be reinforced by the realization that subsidy mail pay will not be forthcoming to perpetuate an uneconomic route pattern. By the same token, the incentive on the part of the acquiring carrier will be to strengthen its route system so as to improve its earning power and its over-all position.

There is no indication in the record that had Western been certain that the profit it would realize on the sale

would be considered "other revenue" it would not have sold the route. In fact, it had no basis for believing otherwise when it negotiated the sale. The immediate objectives of the sale by Western apparently were to obtain funds critically required to avert bankruptcy or receivership and to continue in operation and at the same time to divest itself of a route which Western itself had come to regard as having little long-term value in the development of its system.

During the period of approximately three years since the sale of Route 68, there have been no instances of agreements for the transfer of a carrier's trunk routes presented to us for approval, which might serve as an indication of the validity of Western's contentions regarding incentives for route transfers. The outstanding example of the 3509 merger of two airlines was the recently approved purchase of the assets and business of American Overseas Airlines, Inc., by Pan American Airways, Inc.¹⁶ Since the price paid by Pan American for the properties approximated their book value, it appears that there were sufficient incentives to negotiate this transaction on the part of both parties which outweighed the consideration of a profit. It does not appear, therefore, that the profit motive is such a necessary consideration for the accomplishment of route transfers or mergers as Western would have us believe.

Western argues that consideration of a capital gain from the sale of assets as part of the profit of an airline injects an element of instability into the prospects of long-range profitability as viewed by the investing public and would prevent the industry from attracting the holding capital. The argument is that investment analysis of air carriers concerns itself with the prospect of long range profitability of air transport and not with the carriers' ability to make up their deficiencies in any one year with profits from the sale of routes; and that by including the profit in reducing

¹⁶ North Atlantic Route Transfer Case, Docket No. 3589 *et al*, Order Serial No. E-4410 (July 10, 1950).

need, the investor is given a distorted and unstable impression of the level of normal mail pay, and therefore only normal and recurring elements of revenue should be included. We do not believe that this result will follow from our decision here. For the past period here under review, the rate will pay all losses incurred under efficient and economical management plus a return on investment. The offsetting of capital gains against need does not impair the financial position of the carrier, but rather tends to neutralize the effect of the sale on the net worth. In fixing the future mail rate for Western we have considered only normal recurring non-mail revenues. We believe that an investor looking at both rates will not get a distorted impression of Western's earnings and its long range profitability.

In view of the foregoing considerations, we find that the net profit from the sale of Route 68, amounting to \$1,099,000, is "other revenue" within the meaning of Section 406(b) of the Act, and that Western's mail pay need should be reduced accordingly.

3510 *Reasonableness of Western's DC-3
Maintenance Expense*

Western's level of DC-3 maintenance expense is characterized throughout the period under review by the extent to which it exceeds that of six representative domestic trunk lines operating DC-3 aircraft, either individually, or on the average, particularly in 1946 and 1947. This determination has been made by a comparison of total maintenance expense by type of equipment on an hourly basis, after allocating ground and indirect maintenance expense to equipment types according to the ratio of direct labor dollars expended for each type. The results for Western and the six selected carriers are set forth in Appendix No. 4. The basic question before us is to what extent were the high costs subject to the control of management and, therefore, not allowable for rate-making purposes.

Although Western agrees with the use of the six carriers for the purposes of comparison, it contends that its total maintenance expense for DC-3's and DC-4's combined should be compared with that of the other carriers on the basis of available ton-miles rather than by equipment types on an hourly basis, since this is alleged to be the best overall method for evaluating airline costs; and moreover, indirect expense cannot be allocated properly for Western because its engine overhauls were performed by an outside contractor, Pacific Airmotive Corporation, whereas the six selected carriers performed engine overhauls in their own shops. If an allocation should have to be made, it urges that the ratio of total direct maintenance dollars for each type of equipment be used instead of direct labor dollars, and that any overage of DC-3 indirect maintenance expense in excess of the average of the group of six carriers be offset against the underage of DC-4 indirect expense resulting from a comparison of DC-4 operators. In addition to the distortion caused by farming out its engine overhauls, Western claims

that the direct labor dollar basis of allocating indirect maintenance expense is defective, since it assigns all of the 1945 expense to DC-3 aircraft, although substantial indirect expense was incurred in behalf of the DC-4 equipment program when no direct maintenance expense was charged to DC-4's.

Western's argument for a comparison of combined DC-3 and DC-4 maintenance expense has been advanced before in the *Northeast Case*, where it was rejected as follows (*Northeast Air Lines, Inc., Mail Rates*, 9 C.A.B. 291, 298 (1948)):

Northeast has objected to the use of the comparative DC-3 maintenance costs set forth above on the ground that the allocation process has distorted the accuracy of the basic data, and contends that a more appropriate comparison would be on the basis of maintenance cost per hour flown for all types of equipment combined. This objection obviously is without merit in cases where operations were con-

ducted exclusively by DC-3 aircraft and, in the case of mixed fleets, it is apparent that the average maintenance costs for combination operations with two-engine DC-3 and four-engine DC-4 aircraft could not be comparable from one carrier to another unless the proportionate division of total operations between the two types of aircraft were virtually identical for all carriers compared. Since it is clear from the record that this was not true, it must be concluded that Northeast's proposal that comparison be based upon the combined maintenance costs for all types of aircraft is statistically fallacious.

The allocation of indirect maintenance expense to type of equipment on the basis of direct labor dollars represents the most logical basis under most circumstances to accomplish that purpose and has been used by many industries, including the air carrier industry, as well as by Western itself. Despite Western's assertions to the contrary, the record lends no support whatsoever to the claim that the direct labor dollar basis assigns an unduly high proportion of indirect maintenance expense to DC-3 aircraft. If Western had shown that the ratio of DC-3 labor to total labor would have been less had it performed its own engine overhauls, and that the amount of indirect expense allocable to DC-3's would have been less, then it would be proper to make allowance for this factor. Such a showing was peculiarly within the province of Western, yet, even when specifically requested to do so, it offered no data on the 3512 subject. The only affirmative showing in the record as to the effect on the allocation of indirect maintenance expense to DC-3 aircraft had Western performed its own engine overhauls in 1946 and 1947, was a test made by a witness for Public Counsel on the basis of DC-3 and DC-4 engine overhauls performed by Western in the latter part of 1948 and in 1949. This test indicated that the proportion of indirect maintenance expense allocated to DC-3 aircraft would not have been any less had Western performed its engines overhauls instead of contracting for them on the

outside. Aside from this indication, however, it is clear that the indirect maintenance expense as experienced by Western is more closely related to the direct labor costs of its own organization than to outside repair costs, which reflect in themselves certain indirect costs of the contractor.

In view of the foregoing considerations, we find that the method of allocating indirect maintenance expense to equipment types on the basis of direct labor dollars of expense, the same method that was adopted in the *Northeast* case, is reasonable and proper to apply in this proceeding.

Western contends that although it incurred indirect maintenance expense during the latter part of 1945 in implementing its DC-4 equipment program, nevertheless, the lack of any charges for direct labor on the DC-4's during this period resulted in all indirect maintenance expense being charged to DC-3 aircraft. Although this contention has merit, an abnormal situation of this kind cannot be considered as discrediting the allocation basis we have adopted. Rather it requires that we seek other means for determining the amount of expense that may reasonably be attributed to the DC-4 aircraft in 1945. The record indicates that Western's maintenance personnel devoted considerable time to planning and supervising modifications to eight DC-4's, coordinating the purchasing of five new DC-4's, and provisioning for its new DC-4 fleet, yet Western could not provide a detailed breakdown of the costs involved in this program. Instead, the carrier made a computation of the additional DC-3 maintenance costs incurred in the last four months of 1945 on the basis of the excess unit costs per revenue plane mile for this period over the previous eight months of the year, resulting in an amount of \$150,000, which it alleges should be charged against the DC-4 aircraft.¹⁷ It appears from the evidence that direct costs were incurred in behalf of the DC-4's in preparing the DC-4's for scheduled service as well as in connection with

¹⁷ It should be noted that the amount of \$150,000 is equivalent to the entire indirect maintenance expense for the last four months of 1945.

the approximately 40,000 miles of nonrevenue flying during this period. A more valid basis, therefore, for measuring the bulge in maintenance costs occurring in the last four months of 1945 is believed to be a comparison with the total maintenance costs per revenue plane mile for the same period in 1944. On this basis, the excess expense charged to DC-3 aircraft, which may reasonably be considered as applicable to the DC-4's, amounts to \$74,000, or approximately \$2.00 per hour. This hourly cost has been removed from the 1945 DC-3 maintenance expense of \$30.05 per hour for the purpose of determining the extent of excess DC-3 expense during the rate period.

After allocation of indirect maintenance expense by type of equipment and adjustment of Western's 1945 expense as above, Western's total DC-3 maintenance expense compares to the average of the six intermediate carriers as follows:

| | Total DC-3 Maintenance Expense | | | | |
|---------------------------------------|--------------------------------|---------|---------|---------|---------|
| | 1944 | 1945 | 1946 | 1947 | 1948 |
| Western | \$28.09 | \$28.05 | \$39.02 | \$36.46 | \$26.65 |
| Average of six carriers ¹⁸ | 23.14 | 20.99 | 22.87 | 23.08 | 22.41 |
| Variance | \$ 4.95 | \$ 7.06 | \$16.15 | \$13.38 | \$ 4.24 |

Western contends that there were many factors beyond its control which account for its higher level of expense than the other carriers, the most significant of which are: (1) the inadequacy of the maintenance and operations base at Burbank, California, (2) the necessity of farming out its engine overhauls, (3) the relatively shorter overhaul and inspection periods than the average for the industry, (4) greater engine wear and tear caused by the mountainous terrain along its routes, and (5) the instability of the labor market in and about Burbank.

A review of all evidence of record reveals that Western did not suffer any disadvantage from shorter overhaul and inspection periods when compared to the six intermediate carriers, and consequently, no allowance should be made for

¹⁸ As indicated in Appendix No. 4, these carriers are Braniff, Capital, Chicago & Southern, Continental, Delta, and Mid-Continent.

this factor in evaluating Western's high level of maintenance expense. On the other hand, it is clear that Western was handicapped by the lack of proper facilities at the Lockheed Air Terminal in Burbank and by its inability to expand those facilities to keep pace with its larger volume of operations. Western took prompt action as soon as possible after the war to provide itself with a new hangar at the Los Angeles Municipal Airport, which it occupied in the middle of 1947. Since the additional costs generated by poor facilities did not result from uneconomical and inefficient management, a proper allowance should be made for this factor in the maintenance expense recognized for Western. It appears that the other factors affecting Western's maintenance expense were also beyond the control of management for the greater part of the review period, and that a reasonable allowance should also be provided for these factors.

Although there is no mathematically precise method to measure the impact of the various factors on the level of Western's maintenance expense, we believe that a differential technique is the most reasonable basis for the determination of an allowance for factors beyond the control of Western's management. A differential above the average experience of a representative group of carriers provides a means of relating a reasonable level of expense to Western's own experience as well as that of the group average. Public Counsel's witness has suggested that a differential should be used based on the average of the two years 1944 and 1948. The inclusion of the year 1948 in the differential, however, understates the effect of poor facilities on costs, this being the first full year that Western occupied its new hangar. It appears that the two years 1944 and 1945 are more representative as a base for this differential, since they immediately precede the two years when DC-3 maintenance expense rose to extremely high levels. Although the average cost per hour of maintenance in 1944 and 1945 is \$6.00 above the average of the six carriers, we find that this

is a reasonable differential in view of the adverse factors beyond the control of management which were all present during this period. Thus, the projection of the average 1944-1945 differential into the years 1946 and 1947 reasonably provides a proper allowance over the average of the six carrier group to compensate for the effect of these factors.

In our opinion this technique adequately accounts for all of the above factors that were beyond Western's control and affected its costs in 1946 and 1947. In fact, it seems very probable that various adverse factors contributing to the differential in 1944 and 1945 were present to less degree in 1946 and 1947. Particularly in the latter year, labor conditions had largely been stabilized and Western was able to reduce its maintenance personnel after the move to the new hangar and after the sale of Route 68. Also, after Western had completed its move to Los Angeles Airport in the middle of 1947, the facility factor was eliminated. Moreover, its average DC-3 engine overhaul costs were substantially lower than in the 1944-1945 period.¹⁹

The adjusted DC-3 cost of \$28.05 per hour in 1945 exceeds the average of the six carrier group by \$7.06, which we find to be a reasonable differential for this year. When this is averaged with the \$4.95 excess in 1944 an average differential of \$6.00 per hour results, which we have applied to the six carrier average in 1946 and 1947 as indicated in the table below:

¹⁹ An indication of the liberal allowance provided Western is that full weight is given Western for lack of overhaul facilities in 1947, although the record indicates that it might have been possible for Western to have installed its engine overhaul shop at the time of its move to its new hangar, rather than a year and a half later, and to have used war surplus engines in lieu of overhaul by scrapping the engines after expiration of the operating time. This doubt has been resolved in favor of Western, however, in the application of the differential.

DC-3 Maintenance Expense

| | Average of Six Carriers | Differential | Cost Per Hour | Recognized Expense | Reported Expense | Excess Expense |
|----------|----------------------------|--------------|---------------|-----------------------|---------------------|-------------------|
| 1946 | | | | | | |
| Direct | \$13.69 | \$3.98 | \$17.67 | \$ 640,803 | \$ 897,370 | \$256,567 |
| Indirect | 9.18 | 2.02 | 11.20 | 406,168 | 517,787 | 111,619 |
| Total | \$22.87 | \$6.00 | \$28.87 | \$1,046,971 | \$1,415,157 | \$368,186 |
| 1947 | | | | | | |
| Direct | \$12.85 | \$3.98 | \$16.83 | \$ 374,585 | \$ 478,181 | \$103,596 |
| Indirect | 10.23 | 2.02 | 12.25 | 272,648 | 333,417 | 42,864* |
| Total | \$23.08 | \$6.00 | \$29.08 | \$ 647,233 | \$ 811,598 | \$146,460 |

* Excludes \$17,905 cost of move to Los Angeles Airport recognized as an abnormal non-recurring cost allowable for rate-making purposes. This amount represents the DC-3 portion of total cost of \$44,431, allocated on basis of DC-3 direct labor ratio of 40.3 percent.

As a result of the foregoing, we find that Western incurred excess DC-3 maintenance expense of \$368,186 in 1946, and \$146,460 in 1947, or a total of \$514,646 for the two year period, which should be disallowed from current operating expense.

In our consideration of Western's high level of DC-3 maintenance expense in the Tentative Statement, we recognized that imposition of DC-4 operations over Route 68 on Western's already over-burdened facilities was one of the factors contributing to excess maintenance charged to DC-3 aircraft. The propriety of making an offset of DC-3 maintenance expense against the route profit, which is an issue in this case, is discussed in a later section pertaining to 3518 offsets.

Reasonableness of General and Administrative Expense

A comparison of Western's level of general and administrative expense for the years 1946-1948 indicates that it exceeds the average of a representative group of domestic trunk lines when measured on the basis of either the ratio to all other cash operating expenses, cost per available ton-

mile, or cost per revenue ton-mile. The most appropriate basis of comparison for the purpose of determining the extent to which a carrier's general and administrative expense is excessive is believed to be the ratio of such expense to all other cash operating expenses, since this basis appears to provide the most reliable single measure of the requirement for general management service of which general and administrative expense is largely composed. The units of available and revenue ton-miles appear to be subject to greater distortion than the ratio basis, because the difference in the available capacities of various types of equipment is usually greater than the difference in their operating costs, and the use of revenue ton-miles relates primarily to traffic carried, without giving proper weight to costs relating to production of capacity units. The ratio, on the other hand, provides a synthesis of factors relating both to the operation of a certain capacity as well as to the carrying of traffic. Although the reasonableness of cost levels should be tested on all valid bases, yet a comparison of general and administrative expense on the basis of its ratio to all other cash operating expenses appears to be the most equitable. In addition to the above considerations, we have found this basis to be a valid method for comparing general and administrative expense in other recent mail 3519 rate cases.²⁰

Five of the six carriers with whom Western is compared are the same as used in the comparisons of maintenance expense,²¹ and for the sixth carrier we have substituted National for Continental, since it is one of the closest to Western in volume of operations, and since Continental operated only two-engine equipment during the three-year

²⁰ Southwest Airways Co., Mail Rates, 9 C.A.B. 731 (1948); West Coast Airlines, Inc., Mail Rates, Docket No. 2732, Order Serial No. E-2640 (March 28, 1949); Challenger Airlines Co., Mail Rates, Docket No. 2897, Order Serial No. E-3251 (September 8, 1949); American Overseas Airlines, Inc., *et al.*, Statement of Tentative Findings and Conclusions, Docket Nos. 1666, 1706, 2375, and 4021, Orders Serial Nos. E-3880, 3881, and 3882, (February 7, 1950).
Mid-Continent.

²¹ The carriers are Braniff, Capital, Chicago & Southern, Delta, and

period for which a comparison is made, resulting in a distortion when compared to the high level of Western's operations with DC-4 aircraft. National is omitted from the comparison in 1948, to eliminate any distortion resulting from a strike over its system.

As our later discussion indicates, we have found that Western incurred excess general and administrative expense in 1947 and 1948 amounting to \$161,000 for the two years, based on the ratio method. We have tested the results so obtained by comparing Western with the same six carriers on the basis of costs per available and revenue ton-miles, which produces excess expenses for the two years of \$208,049 and \$136,901, respectively, for the two bases. Since both bases have some validity as a measure of the reasonableness of general and administrative expense, we have averaged the two amounts of excess expense, resulting in \$172,000. This amount is approximately the same as the excess determined by the use of the ratio method.

Western contends that Continental should be used as well as National for the reason that the same carriers should be included in both maintenance and general and administrative expense comparisons, and moreover, the comparison should be made on the basis of available ton-miles. In addition to the merits of the ratio method as mentioned above, there is an indication that the use of available ton-miles would create a greater disparity in results as between carriers with variations in volume of operations by two and four-engine equipment than would result from the ratio method. The adoption of Western's method would result in an excess expense of only \$43,000. If both Mid-Continent and Continental, which operated only DC-3 aircraft, are used in the comparison, in addition to the five other carriers operating a mixed fleet of DC-3's and DC-4's, evidence in the record indicates that it would be valid to use the cost per available ton-mile of Western and Inland combined, since Inland also operated DC-3's during 1947 and 1948, in addition to the fact that the major part of Inland's general and administrative expense was incurred by West-

ern and allocated to Inland. The result of a comparison on this basis is an excess expense of \$167,000, which is only slightly higher than the amount determined by the application of the ratio method. Even if we accepted Western's group of carriers and the available ton-mile basis of comparison, (and using Western-Inland combined) the results support the validity of the ratio method.

Western also contends that it is improper to compare its costs, either maintenance or general and administrative, with those of other carriers which have been adjusted by the Board in other proceedings to eliminate amounts of expense in excess of a level considered fair and reasonable for rate-making purposes. It reasons that adjusted costs do not represent the actual experience of a carrier which must be used as the basis of comparison. We consider such a proposition to be entirely without merit in the process of determining costs allowable for rate purposes, since we would

be required to include excess costs previously found
3521 to exist in the base used to measure the extent of excess costs in the carrier under consideration. Although it may be necessary in some cases to use only reported costs of carriers in comparisons because we have had no opportunity to make a detailed determination of the reasonableness of such costs, this situation cannot be accepted as a bar to the use of adjusted costs when they exist.

In making a comparison of any kind, consideration should be given first to any factors which may be isolated and evaluated as to their effect on the cost level. We recognized in the Tentative Statement that Western had a unique situation in the high level of property taxes it is required to pay on property in Los Angeles County, which was substantially above that of other intermediate carriers. Accordingly, we have made an allowance, on the basis of available ton-miles, for property taxes in excess of the average of the six selected carriers in the amounts indicated in the Appendix. We also made adjustments in the Tentative Statement, disallowing amounts of contributions and entertainment expense which were readily ascertainable for the years 1945-

1947 in the amount of \$43,000. An adjustment was made to 1946 expense to capitalize \$12,000 of preoperating expense relating to Route 68, which was charged to current expense, and to provide for the amortization of this amount over a five-year period. One other adjustment was included in the Tentative Statement in 1947, increasing the allocation of general and administrative expense to Inland in the fourth quarter, when the ratio of cash operating expenses of Inland to the total for the system increased from 15 percent to 23 percent following the sale of Route 68. This adjustment has been made here also in approximately the same amount as previously. Western's final results for the year 1948 include a revision in the allocation to Inland, although in an amount which leaves Inland's expense for the year in excess of 23 percent of the system total, after reflecting our adjustment to 1948 expense. We have revised Inland's general and administrative expense downward to an amount consistent with Western's recognized expense. There is no issue with respect to the above adjustments in this proceeding.

After reflecting all of the foregoing adjustments, we find that Western's general and administrative expense is above the average of the six selected carriers, measured on the ratio basis, by 0.61 percentage points in 1946, 1.72 in 1947, and 1.57 in 1948, as indicated by the table below:

**Ratio of General and Administrative Expense to
All Other Cash Expenses**

| | 1946 | 1947 | 1948 |
|------------------------|--------|-------|-------|
| Braniff | 10.16% | 9.46% | 8.42% |
| Capital | 9.75 | 8.79 | 7.38 |
| Chicago & Southern | 11.28 | 10.10 | 8.64 |
| Delta | 7.99 | 8.70 | 9.11 |
| Mid-Continent | 10.64 | 9.82 | 9.47 |
| National | 9.33 | 8.04 | 8.23* |
| Average | 9.86% | 9.15% | 8.60% |
| Western as adjusted | 10.47 | 10.87 | 10.17 |
| Variance above average | .61 | 1.72 | 1.57 |

* National omitted in 1948 because of possible distortion from strike. Since Western's ratio of 10.47 percent in 1946 is lower than two of the selected carriers, and within a reasonable range

of the average, we believe that no additional amounts of expense should be disallowed in 1946. In 1947 and 1948, however, Western's ratio is above that of any of the carriers in the group and does not fall within a reasonable range. We believe that it would not be unreasonable to expect that Western could have attained a ratio in these two years that would bear the same relationship to the group average as existed in 1946, when we recognized a ratio of expense approximately six percent above the average, after preliminary adjustments to Western's expense. Accordingly, we recognize a level of general and administrative expense for Western which is 9.72 percent of all other cash expenses in 1947, and 9.15 percent in 1948. We find, therefore, that Western incurred excess expense of \$92,550 in 1947, and \$68,625 in 1948, which should be removed from current operating expense. It appears, however, that the entire amount of \$161,175 should be offset against the profit from the sale of Route 68, as we shall discuss in the following section.

3523 *Offsets Against the Profit From Route 68*

We indicated before in our Tentative Statement that Western incurred certain costs which should properly be offset against the profit from the sale of Route 68, since they had their incidence in Route 68 and made it possible, in large measure, for Western to realize the profit it did from the sale of the route. These costs may be grouped as follows in the order of their importance dollar-wise: (1) divestment costs arising from the lag in reducing costs in accordance with the reduction in volume of operations; (2) DC-3 maintenance costs that became excessive through the operation of DC-4 aircraft; and (3) miscellaneous items primarily related to the development and sale of the route. Although Western and Public Counsel are in substantial agreement on the amount of the offsets, the Postmaster General has objected to all offsets except an amount of \$31,000 relating to miscellaneous costs of the sale.

1. Divestment Costs

Following the sale of Route 68, Western's unit costs related to ground and indirect expense accounts rose sharply as a result of the sudden shrinkage in operations, and this trend carried over into 1948 for most expenses. The extent of the shift in Western's scale of operations is clearly shown by the percentage change in revenue and available ton-miles in the fourth quarter 1947, and in the first six months of 1948, as compared with the average of six carriers ²² in the table below:

| | Percentage Change in Revenue | | Ton-Miles Operated | |
|------------------------------------|------------------------------|---------------------|--------------------|---------------------|
| | Western | Six Carrier Average | Western | Six Carrier Average |
| 3rd to 4th quarter, 1947 | -50.6% | -7.2% | -30.1% | -7.9% |
| 1st 6 mos. 1947 to 1st 6 mos. 1948 | -46.1% | +1.1 | -27.3 | +5.4 |

²² Braniff, Capital, C & S, Continental, Delta, and Mid-Continent.

3524 It is reasonable to expect that there was an unavoidable lag required for adjustments in organization and expense levels to meet the sharp curtailment in operations, but the duration of the period cannot be determined with any degree of precision because of the vast number of items which make up the amounts involved. The Postmaster General does not dispute the principle of divestment costs. He contends rather that in the absence of specific details as to each and every individual cost entering into the accounts in issue, divestment costs can neither be established nor assigned to Route 68. In view of the virtual impossibility of obtaining the data that the Postmaster General would require and the further fact that the record contains ample evidence upon which the determination of divestment costs may be predicated, we find this contention to be without merit. The data in the record indicates that the lag in adjusting the level of most of the ground and indirect expenses carried over from the fourth quarter of 1947 well into 1948. When Western's unit costs for the periods before and after the sale of Route 68 are compared

with the average costs of representative groups of carriers, it is found that, while Western's expenses were generally at a reasonable level for the three quarters prior to the sale, they increased to a high level for the fourth quarter concurrent with the sharp cut in the level of operations and continued high in relation to the average of the selected carriers until approximately mid-1948. To the extent that the excessive nature of these expenses appears to be the consequence of the sale of the route rather than of uneconomical and inefficient management, it is reasonable to conclude that the excess expenses were in the nature of divestment costs, which would not have occurred but for the route sale, and which should be offset against the profit from that sale rather than charged against current operations not directly responsible for the incidence of those costs.

3525 As indicated previously, Western's general and administrative expense was excessive by \$92,550 in 1947, and \$68,625 in 1948. While Western's expense appears to be excessive in the first half of 1947, the ratio to all other cash expenses was within the same range of the six-carrier average which we found to be reasonable for 1946, and reflected a downward trend in line with the experience of the other carriers. This trend was reversed in the third quarter of 1947, which included the half month of September following the sale, and more sharply in the fourth quarter as a consequence of the drop in volume from the elimination of Route 68 operations. Western's adverse expense level extended through mid-1948, and into a portion of the third quarter. As Western progressed into 1948, however, its general and administrative expense continued to decrease, and the disparity in its ratio lessened; until by the fourth quarter its expense level was no longer excessive. Thus, it is plain that the incidence of Western's excess expense coincided with the divestment of Route 68. In view of all the foregoing, we find that the entire amount of the excess, \$161,175, should be offset against the route profit.

In the case of ground operations expense, Western's expense compared favorably with the average of other car-

riers for the first three quarters of 1947, and throughout the year 1948. In the fourth quarter of 1947, however, Western's expense substantially exceeded the average. The record supports the finding, therefore, that divestment costs amounted to \$70,000 in that quarter. Similarly for merchandising expenses, consisting of passenger service, traffic and sales, and advertising and publicity expenses, application of the same technique reveals that Western incurred excess expense of \$90,000 in the fourth quarter of 1947, and \$64,000 in the first six months of 1948, which should properly be considered divestment costs, since they arose in the period immediately succeeding the route sale.

Accordingly, we find that the total amount of divestment costs which should be offset against the route profit 3526 is \$385,175.

2. Excess DC-3 Maintenance Expense

The most serious difficulty that confronted Western's management during most of the review period was without a doubt the lack of adequate facilities, particularly for its maintenance operations. This critical situation was intensified after the inauguration of service with the DC-4 aircraft in 1946. The excessive expense level that resulted became apparent through expenses chargeable to DC-3 operations. After consideration of all data of record, we believe it is reasonable to conclude that maintenance expense which became excessive was due in large part to the burden of operations of DC-4 aircraft over Route 68. The increase in efficiency of maintenance operations following the divestment of Route 68 is clearly illustrated by the sharp drop in DC-3 maintenance expense from \$36.45 per hour in 1947 to \$26.65 per hour in 1948. Although the new hangar facilities accounted for a large part of this improvement, the withdrawing of Route 68 operations undoubtedly had an effect. Marked improvement was shown also in total DC-4 maintenance expense, which was \$70.13 per hour in 1947, and declined to \$50.39 in 1948, the lowest of all domestic trunk lines except the Big Four.

In circumstances such as we find here, where the development of a route or similar operation results in abnormal costs, we believe it is proper from a rate-making point of view to consider these costs as capable of being amortized or recoverable over an extended period of time from the continued operation of the route. This possibility has been ruled out here because the transfer of the route has destroyed the basis for amortization. Consequently, these abnormal costs, which were a by-product of the operation of Route 68 and contributed to the development of its earning power, should be matched against the benefits accruing from the route sale.

3527 The determination of the amount of excess DC-3 maintenance expense to be offset against the route profit is largely a matter of judgment, since the record has not developed any precise method for deriving such an amount. On the basis of the facts in the record, Public Counsel has urged that the maximum amount of offset should be no more than \$283,000. Western claims that \$300,000 is the amount of offset for the two years 1946 and 1947, based on the alleged expense of \$150,000 applicable to the DC-4's in 1945, which computation we have already rejected. The Postmaster General contends that there is no reason why Western should be provided with an allowance of costs in excess of the differential above the six carrier average. The differential is based, however, on 1944-1945 operations, whereas the impact of DC-4 operations on Western's costs occurred in 1946 and 1947. After consideration of all evidence of record, the amount of excess expense of \$514,646, and the fact that DC-4's were operated on the coastal routes during 1946 and 1947 as well as on Route 68, it is not unreasonable to consider that the amount of \$283,000 should be offset against the route profit. Thus, the remaining excess DC-3 maintenance expense that has been disallowed from operating expense is the amount above the level reasonably attainable under economical and efficient management.

3. Miscellaneous Offset Items

The remaining items at issue with respect to offsets against the route profit and the related amounts as indicated in the record are listed below. All of these items, except the last two, were considered to be proper offsets in the Tentative Statement, but were objected to by the Postmaster General in his formal answer thereto.

3528

| | |
|--|-----------|
| DC-6 cancellation charges | \$ 65,216 |
| Miscellaneous costs of sale | 32,389 |
| Unamortized preoperating and training expense | 128,794 |
| Unamortized extension and development expense | 25,636 |
| Depreciation on flight training equipment | 52,523 |
| Depreciation on excess R-2000 engines | 32,309 |
| Abnormal loss estimated on retirement of DC-4 nonrotatable spare parts | 104,000 |
| Loss on engine overhaul equipment | 69,745 |
| Loss on Denver reservations system | 856 |

With respect to the DC-6 cancellation charges, the Postmaster General contends that Western was purchasing these aircraft in anticipation of a route extension to Chicago. The record supports Western's claims, however, that pressurized aircraft were required to provide adequate service over Route 68 because of the high operating altitudes and in order to compete successfully had it retained the route. Therefore, these costs as well as the miscellaneous costs of the sale are considered to have been a proper charge by Western against the sale price in the same amounts as indicated above.

Both of the items of preoperating and training expense and extension and development expense involve the same treatment, in that the expenses were incurred in obtaining and inaugurating service on Route 68, and the expenses were charged off to current expense by Western and capitalized in the present proceeding. Capitalization and amortization of such expenses is consistent with our policy in many previous cases and cannot be considered as a new procedure in the rate-making process. We indicated in the recent *Continental* case,²³ however, that if such expenses have

²³ *Continental Air Lines, Inc., Mail Rates*, Docket No. 3281, Order Serial No. E-4332 (June 21, 1950).

been written off to current expenses in the period prior to the date of petition, they cannot be considered in determining the mail rate for the later period. If proper
3529 and reasonable development expenses are deferred by a carrier and amortized on a basis that will create a charge to the period under review, we would consider the amortization as a proper charge to current expense. A portion of the total of \$36,831 of Route 68 extension and development expenses falls into this category, \$15,098 having been written off by Western prior to May 1, 1944. Accordingly, we will recognize only the amount of \$21,733 as applicable to the review period. Amortization of this amount from April 1, 1946, the date service was inaugurated, until September 15, 1947, the date of the route sale, on the basis of a five-year period, results in charges to expense of \$6,339, leaving an unamortized balance of \$15,394 to be offset against the route profit. The amount of preoperating and training expense capitalized has been reduced from \$181,827 to \$161,072 in accordance with evidence that DC-3 training applicable to Route 68 totaled 1,125 hours, and DC-4 training hours were 611 or 48.69 percent of the total, determined from the percent of total DC-4 miles operated over Route 68 to the total for the system for the last nine months of 1946. Amortization on the same basis as extension and development expense equals \$46,978, and the balance of \$114,094 is offset against the profit from Route 68.

In our Tentative Statement we offset against the route profit depreciation pertaining to DC-3 and DC-4 flight equipment, which Western claims was necessary to place Route 68 into operation in the shortest possible time. The Postmaster General contends that recognition of depreciation on training equipment is contrary to Board policy that depreciation on aircraft obtained for scheduled revenue service shall commence as of the effective date such aircraft are placed in regular service. It does not necessarily follow that depreciation may never be recognized on aircraft purchased for training only, if the aircraft were required under the circumstances. Although we have not recognized

the depreciation in question as a charge to operating expense, yet there is merit to Western's contention that the equipment made a contribution to the route's earning power and was a factor in enabling Western to realize the profit it did from the sale. Consequently, we believe that this depreciation may properly be offset against the profit.

Although in the Tentative Statement we held that the depreciation on the excess R-2000 engines should be offset against the route profit, it now appears from the record that the abnormal failure rate of these engines prompted their purchase as an insurance factor. Also the farming out of engine overhauls reduced to some extent the control of management over the availability of spare engines, necessitating a higher than average number of spares. Many of these engines were cannibalized for spare parts to maintain others in operation. We find, therefore, that the amount of \$32,309 depreciation on R-2000 engines should be recognized as normal operating expense and not offset against the route profit.

We have allowed Western to accrue a reserve of \$200,000 against the estimated loss from the retirement of DC-4 non-rotatable spare parts. This amount is approximately equivalent to that allowed other DC-4 operators and is not in issue in this proceeding. Western has claimed that it will sustain an additional loss of \$104,000 on the ground that the major portion of its inventory was purchased to support the operation of Route 68, and that it has been impossible to reduce this inventory to a normal level after the sale of

the route without incurring a loss. The Postmaster
3531 General urges that no additional allowance should be made for such a loss, since Western indicated at the hearing in the *Acquisition* case²⁴ that it had made a profit selling DC-4 parts, and that, moreover, Western

²⁴ United-Western, Acquisition of Air Carrier Property, 8 C.A.B. 268 (1947).

transferred \$222,000 of spare parts to United at the time of the route sale. It appears more reasonable to us, however, to accept the present estimate of loss rather than a statement made in early 1947 as to the market for certain unidentified parts at that time. In our opinion these parts are sufficiently related to the operation of Route 68 so as to warrant the offset of the amount of \$104,000 abnormal loss against the profit from the sale.

An additional amount of \$69,745 is in issue as an offset against the route profit, representing the net loss on retirement of an engine washing system, test cells, and other engine overhaul equipment in 1947. The amount is computed from a loss of \$74,345 reported in 1947, less revenue of \$4,600 from salvage of parts in 1948. Western contends that this equipment, purchased for the installation of an engine overhaul shop in its new hangar, became surplus after the decision to sell Route 68, since an overhaul shop of a size to utilize this large equipment was not feasible for the reduced volume of operations. The facts of record and the timing of the retirement sufficiently relate this equipment to the disposal of Route 68 so as to warrant the inclusion of the loss as an offset to the profit, even though it cannot be recognized as a normal loss from retirement as used and useful air carrier property.

A loss of \$856 was sustained by Western from the cancellation of a partially installed reservations system at 3532 Denver following the sale of Route 68. This appears to be clearly a cost to Western related to the sale of the route and the disposition of equipment used in its operation and, therefore, should be offset against the route profit as a cost of sale.

The total amount of the offsets against the route profit is, accordingly, \$1,122,392, which includes \$97,605 of charges by Western against the gross sale price. The net profit considered "other revenue" becomes \$1,099,130, and we have applied this amount as a reduction in Western's mail pay need as required by Section 406 (b) of the Act.

Net Gain from Retirement of Operating Property

In addition to the elimination of the loss on engine overhaul equipment in 1947, discussed above in connection with the offset against the route profit, there are two other adjustments which affect the gain of \$116,000 from the retirement of operating property recognized in the Tentative Statement. In the last quarter of 1948, Western sold three DC-3 aircraft, reporting a profit of approximately \$70,000. After reflecting the adjustment in book value of DC-3 equipment, however, resulting from the extension of service life from May 1, 1944 to June 30, 1949, the gain is reduced by \$66,404. Consequently, instead of there being a reported gain of \$14,940 from the retirement of operating property in 1948, there is a loss of \$51,464 which must be taken into account.

Western claims that there is an additional loss of \$12,162 in 1948, on the retirement of engines which should be recognized. Part of this total is represented by a billing error of \$2,212 on an engine purchased from the War Assets Administration, necessitating that Western make an additional payment of this amount. Since the engine has been sold, the loss on the sale should be increased by the 3533 higher cost price. The remaining amount of \$9,950 represents the loss on the disposal of engines after the sale of Route 68, which was recorded in account 7187, gain or loss from the sale of nonoperating property. Since these engines were once operating property, we can see no reason for not recognizing the loss therefrom, which will serve to reduce the gain we are recognizing as "other revenue". As a result of these adjustments, the net gain from the retirement of operating property becomes \$155,192 and, accordingly, Western's need is reduced by this amount.

Number of Aircraft Required September 1-December 31, 1948

In the Tentative Statement we disallowed a total of \$96,873 depreciation on DC-3 and DC-4 aircraft in the last

four months of 1948, in view of Western's program for the replacement of this equipment by the Convair 240 starting September 1, 1948. The introduction of the Convairs into service was not as rapid as had been anticipated by reason of mechanical difficulties and modifications which resulted in the removal of many of the Convairs from service after a short period of operation.²⁵ The daily record of operations for each Convair reveals that none of the three aircraft assigned to scheduled service in September were utilized the full month; one aircraft being in operation 16 days; the second, 13 days; and the third, 19 days. During 3534 this time Western had available and consistently operated the eight DC-3's and the five DC-4's which comprised its operating fleet prior to September 1, 1948, and with which it was able to complete 99.4 percent of scheduled service in the peak month of August. In October, Western effectively operated three Convairs, except for the first two days when only one Convair was in operation, and therefore, for all practical purposes the month of October should be considered the initial month of operations with Convair aircraft for rate-making purposes. Also in November and December, because of the intermittent Convair operations, we believe that three aircraft is the maximum number of Convairs that should be recognized. These Convairs would have been sufficient to provide a reduced scale of Convair operations on the coastal route during this introductory period, and, together with the DC-3 and DC-4 aircraft which we recognize, would give Western ample coverage for all scheduled and nonscheduled operations which it performed. The total number of aircraft by type

²⁵ Western attempts to draw an analogy between its difficulties with the Convairs and our policy for recognition of grounding costs tentatively set forth in the Big Four Mail Rate case, Docket No. 2849, Order Serial No. E-2862 (May 25, 1949), where we treated estimated grounding costs of large amounts as developmental costs and amortized them over a five-year period. It is clear from the record in this proceeding, however, that the grounding principle is inapplicable here for a number of reasons, including primarily the fact that Western's Convairs were not actually grounded, but were successively removed from service for various modifications. Moreover, as we indicate later on in our discussion, the depreciation disallowed on the Convairs will be recoverable in later years.

recognized for the four months September-December 1948, is as follows :

| | <i>Sept.</i> | <i>Oct.</i> | <i>Nov.</i> | <i>Dec.</i> |
|--------|--------------|-------------|-------------|-------------|
| DC-3 | 8 | 7.6* | 7 | 6.9* |
| DC-4 | 5 | 5 | 5 | 5 |
| CV-240 | 0 | 3 | 3 | 3 |
| | <hr/> | <hr/> | <hr/> | <hr/> |
| Total | 13 | 15.6 | 15 | 14.9 |

*A fraction of an aircraft is recognized in October and December since Western sold one DC-3 on October 19 and a second DC-3 on December 28, 1948.

Recognition of the above number of aircraft is consistent with our policy of not allowing duplicate aircraft, yet provides for the introduction of a new aircraft type along with the operation of the old fleet until such time as 3535 the new aircraft have been fully tested and can be relied on as a permanent replacement in the fleet. It is recognized that the permanent displacement of the old aircraft fleet must be delayed until such time as reasonable assurance of reliable performance of the new aircraft type has been established by actual operating experience over the carrier's route system. Not only will public confidence in new aircraft be assured by this testing, but the public interest also requires that the mail pay not be burdened by depreciation charges on aircraft that are not used and useful for the operations performed. Accordingly, we have disallowed depreciation on Convair aircraft in excess of three as indicated above, amounting to \$37,058, as a charge against operations in the last four months of 1948. Western will suffer no real loss in Convair depreciation, however, since the future mail rate under which Western is now operating reflects depreciation on the entire fleet of ten Convair aircraft from January 1, 1949.

Miscellaneous Adjustments to Western's Break-Even Need

Operating results for the year 1948 as set forth in the Tentative Statement were based on estimated revenues for

the last quarter and estimated expenses for the last six months. We have revised 1948 data, accordingly, to incorporate actual results as shown in Appendix No. 1. In addition to these adjustments, we have reduced 1948 incidental revenues by \$14,000, which was accrued by Western as a result of a reduction in the billing price of two Convair 240's to reflect hours logged on the aircraft by the manufacturer at time of delivery. We have applied the \$14,000 to the original cost of the aircraft, reducing Convair investment by this amount and eliminating \$800 of depreciation. These adjustments are not contested.

3536 One further adjustment to results in the Tentative Statement is required to revise the loss reported on three DC-3 aircraft which crashed in 1946. The extension in the service life of DC-3 aircraft increased the book value of these aircraft by \$77,000 at the time of the crash, which increases the loss reported by Western in the injuries, loss, and damage account of flying operations expense.

Western's Break-Even Need

After giving effect to all of the foregoing adjustments, we find that Western's need for mail pay for the entire past period before the deduction of "other revenue" is \$3,341,000; but after crediting revenue of \$155,000 from the sale of operating property and the net profit of \$1,099,000 from the sale of Route 68, break-even need becomes \$2,087,000 equal to 6.99 cents per revenue plane mile flown in scheduled service.

Inland's Break-Even Need

The adjustments to Inland's operating results are set forth in Appendix No. 2, reflecting changes from the Tentative Statement required by the use of actual 1948 results and revisions in certain allocations from Western. We have recognized break-even need for the period April 1, 1947, through December 31, 1948, in the amount of \$858,000 equal to 21.2 cents per revenue plane mile flown in scheduled service.

Adjusted Investment of Western and Inland

The principal adjustments to investment of the two carriers recognized in the Tentative Statements apply to working capital for the purpose of revising the previous adjustments for additional temporary mail pay received by the carriers. Western's working capital had been increased in the years 1946-1948 to reflect the additional temporary mail pay of \$975,000, less applicable income tax, spread
3537 equally over the three-year period. The effect of the reduction in temporary mail pay of \$671,474 we have now determined to be required is to revise the additional mail pay applicable to the review period to \$303,500, which we consider to be related to the year 1948, in place of the \$975,000 previously awarded and reported by Western in its balance sheet of December 31, 1948. The effect of these adjustments is to eliminate the allowance for additional mail pay as reflected in our Tentative Statement as well as the effect of the mail pay as reported by Western in 1948, and to add the amount of \$85,000 to the average working capital in 1948. This amount is the average effect of the revised additional mail pay of \$303,500 less approximately \$134,000 for Federal income tax provided in accordance with the revised method for computation of constructive tax described in the following section. We have made a further adjustment to working capital to eliminate the accrued liability for income taxes for all years in the review period, except the amount for 1948 indicated above, since Western had no other tax liability during the review period. Because of the reduction in mail pay of Western, it is necessary to reduce the allocation of working capital to Inland from \$90,000, as indicated in the Tentative Statement, in 1948 to \$68,000. The amounts of the foregoing adjustments are set forth in Appendix No. 5.

Aside from adjustments to operating property and equipment investment to reflect final reported data for Western, a major revision from the Tentative Statement is necessary to recognize all of the investment in DC-3 and DC-4 equip-

ment and to eliminate all Convair aircraft except the three recognized during the introductory period, along with a pro-rata share of spare engines and parts. The net decrease amounts to approximately \$100,000. Other minor adjustments are indicated in the Appendix.

The only adjustment to Inland's investment is to reduce working capital to reflect the reduction in temporary mail pay of \$76,000.

It is customary to allow a return of seven percent per annum for a past period on investment recognized for rate-making purposes, and the allowance of this rate of return here is uncontested. Applying this to the adjusted investment of the two carriers, the return on investment becomes \$1,359,000 for Western, and \$108,000 for Inland.

Federal Income Taxes

As a corollary to the determination of the return on recognized investment, it has been customary in past cases to provide for Federal income taxes on the constructive profit in order to insure that the carrier will realize the return to which it is entitled, on the assumption that the carrier is liable for a tax on the full amount of the profit. The provision for income taxes for Western and Inland was proposed on this basis in the Tentative Statements. The propriety of a tax allowance so constructed was raised by Public Counsel in this proceeding and in all recent mail rate cases,²⁶ and is now before us for decision.

²⁶ This issue was raised in Pan American's Transatlantic Mail Rate Case as indicated in our Amended Statement of Tentative Findings and Conclusions, Order Serial No. 4561, issued August 25, 1950. Pan American filed a petition for leave to file a Memorandum to the Board as Amicus Curiae, in connection with the tax issue in this proceeding. This has been granted and the Memorandum of Pan American has been filed and considered in this proceeding. We also adopted the revised method for computing the constructive income tax allowance, the same as set forth herein, in the Statement of Tentative Findings and Conclusions for Piedmont Aviation, Inc. (Docket No. 3250, Order Serial No. E-4663 (September 27, 1950)). The Postmaster General has formally objected, however, to the proposed tax allowance in both of the above Tentative Statements.

It has become apparent that the constructive tax allowance as applied in the past has sometimes been in excess of the carrier's actual tax liability on the income from the operating entity for which mail rates were fixed, primarily because of the difference in the type and amount of expenses recognized for tax purposes in contrast to those allowed for rate-making purposes. It is clear from the record in this proceeding that the allowance in the Tentative Statement would greatly exceed Western's actual tax liability. The granting of Western's request that the income tax be computed in the manner proposed in the Tentative Statement would in fact provide Western with a windfall allowance for taxes not actually paid.

The ideal policy to follow would be to provide in the mail pay for only that amount of income tax for which liability can be determined from analysis of income tax returns as urged by Public Counsel and the Postmaster

General. In practice, however, basic difficulties might well be encountered in the administration of such a policy. For example, there are likely to be differences between the corporate entity for rate purposes and for tax purposes, as has been pointed out by Pan American, which has different mail rates for each of its divisions but files only one tax return. Also the many variations in accounting policy required for rate purposes in contrast to that followed in tax matters render determination of exact actual amounts of tax extremely difficult.

Although the determination of actual tax liability is not considered feasible, we are of the opinion that a method that will more closely approximate that tax should be followed, which is relatively simple to apply and which provides a suitable means of relating the results obtained for rate-making purposes to the requirements for payment of income taxes. In this method, the constructive profit before taxes, as determined from the allowable return on investment, is reduced by the amount of expenses actually incurred by the carrier which will never be recognized for mail rate purposes but are considered as expenses deducti-

ble for tax purposes. These expenses will include those disallowed as the result of uneconomical and inefficient management and those not allowable for rate-making purposes, such as entertainment and contributions expense, disallowed extension and development expense, interest expense, and other nonoperating expenses which are unrelated or unnecessary to the air transport operation. Adjustments for rate-making purposes which merely have the effect of shifting the incidence of expense from one rate period to another, such as adjustments in depreciation rates or the deferment of certain items taken by the carrier as current expense for tax purposes, would be disregarded in making this tax adjustment, since over a period of time the amounts of

3540 such expense recognized for mail rate and tax purposes will be equalized. The consistent application of our tax policy, while it may provide a lower or higher amount than the tax paid by a carrier in any year, will insure that over an extended period no windfall will inure to the carrier, but that the full amount of the tax will be provided.

As a result of the application of the above method to the facts of this case pertaining to Western, we have allowed provision for taxes in the mail rate of \$134,686, as set forth in Appendix No. 7.

The issue of the proper income tax allowance is the only one before us which directly involves Inland, and which affects the findings in the Tentative Statement relating to Inland, aside from changes in the amount of expenses allocated from Western, and from the use of reported results for 1948. The application of the revised method for computation of income taxes results in an allowance of \$51,000. The basis for this computation is shown in Appendix No. 8.

Determination of Mail Rates

After reflecting all of the adjustments required by our decisions on the issues in this proceeding, we find that the fair and reasonable compensation for the transportation

of mail by aircraft for the entire past period for each carrier is as follows :

| | Western May 1, 1944- December 31, 1948 | Inland March 28, 1947- December 31, 1948 |
|----------------------------------|--|--|
| Break-even need | \$2,087,000 | \$ 858,000 |
| 7 percent return on investment | 1,358,840 | 107,730 |
| Provision for Federal income tax | 134,686 | 51,063 |
| Total | <u>\$3,580,526</u> | <u>\$1,016,793</u> 6,000* |
| Total Mail Pay Requirements | \$3,580,526 | \$1,022,793 |
| Temporary mail pay received | <u>4,252,000</u> | <u>1,099,000</u> |
| Excess Mail Pay | \$ (671,474) | \$ (76,207) |

* To provide for mail pay applicable to the last four days of March, 1947, which amount is not contested.

3541 The mail pay awarded to Western is equal to 12.0 cents per revenue plane mile in scheduled service and 99.4 cents per mail ton-mile. Inland's mail pay is equal to 24.9 cents per revenue plane mile.

Conclusion

As the result of our determination of fair and reasonable mail pay in this proceeding, we have found that Western and Inland have received an overpayment of temporary mail pay of \$671,474 and \$76,207, respectively, which is due and owing to the government. The method for repayment of these amounts is not our concern here, but that of the carriers and the Post Office Department. In considering the existence of the excess mail pay, it should be noted that temporary mail rates are not intended as substitutes for final mail rates since sufficient time does not exist for full analysis and necessary procedural steps to process a final rate. It is for this reason that we always include in our temporary rate orders the proviso that the proceeding remain open pending the determination of final rates, which may be higher or lower than the temporary rates. Although this is the first instance where we have issued a final order finding that a carrier has received excess mail pay, yet we have signified our intention to do so in the mail rate cases

concerning the international operations of Trans World Airlines, Inc., and Northwest Airlines, Inc., by the issuance of Orders to Show Cause²⁷ either reducing the temporary mail rate previously received or indicating that the temporary mail rate being modified was excessive for a prior period.

A review of the various factors which contributed to the excess mail payments in this proceeding is believed to be appropriate in order to indicate that the excess represents a provision for expenses which were never incurred by Western or Inland. The temporary rate was originally awarded as an approximation of a final rate, even though it was known that Western, Inland, and the Postmaster General had filed objections to the Tentative Statement and that a formal hearing would be necessary. This action was taken, however, after the carriers had petitioned for immediate relief because of their critical financial position. Over two-thirds of the excess mail pay to Western, or \$471,000, represents a reduction in the Tentative Statement allowance for Federal income taxes from \$606,000 to \$134,686 as a result of the revision in our tax policy to eliminate the provision for a cost that Western did not incur. Except for a decrease of \$8,000 in the return element, the remainder of the excess payment amounting to \$192,000 comes about primarily from the use of actual 1948 data instead of Western's estimates. The primary effect of Western's lower costs in the last half of 1948 was to reduce the amount of the divestment costs offset against the profit from Route 68, and thus, to increase the amount of the route profit considered "other revenue" which has been deducted from Western's mail pay need. Before crediting "other revenue" we have recognized an increase of \$152,000 in Western's break-even need over that set forth in the Tentative Statement.

²⁷ Transcontinental and Western Air, Inc., Transatlantic Mail Rates, Docket No. 2375, Order Serial No. E-3551 (November 14, 1949); Northwest Airlines, Inc., Trans-Pacific Mail Rates, Docket No. 2539 *et al*, Order Serial No. E-4495 (August 7, 1950).

The revised findings which create the excess mail pay for Inland are due in large part to the actualization of 1948 operating results, which brought about an increase of \$26,000 in revenues and a decrease of \$21,000 in expenses. The decrease in tax allowance of \$20,000 and in the return on investment of \$9,000 make up the balance of the \$76,000 excess mail pay.

Thus, in summary, the excess temporary mail pay resulting from our decisions on the issues in this proceeding represents expenses which were assumed to exist but
 3543 which did not in fact eventuate. The amount of mail pay remaining after elimination of the excess fulfills the break-even need requirements of the carriers as we have determined them and provides for a return on investment which we have customarily allowed carriers for a past period.

An appropriate order will be entered.

Ryan, Vice Chairman, Lee and Adams, Members of the Board, concurred in the above opinion. Jones, Member, filed the attached concurring and dissenting opinion. Rentzel, Chairman, did not take part in the decision.

3544 JONES, MEMBER, CONCURRING AND DISSENTING:

I do not agree with the decision of the majority to treat Western's profit from the sale of Route No. 68 as "other income," thereby requiring it to be offset against mail pay needs, and in effect, recaptured by the government.

While it is true that this action will result in a substantial reduction in the specific Federal subsidy requirements of Western, it is my belief that this particular situation involves policy considerations sufficiently important to outweigh such immediate and specific benefits, and to require a contrary decision. It is, I believe, a "penny-wise and pound-foolish" decision. It is a "short view" decision. Our objective should be the reduction or elimination of the Federal subsidy requirements for our whole nationwide air transportation system, and I believe this policy decision of

the Board will make this objective more difficult to achieve.

For several years the Board, both individually and collectively, has expressed concern over certain illogical aspects of our air route system and the growing burden of subsidies in part attributable to them. It appeared possible to correct abnormalities in the route pattern through voluntary route transfers, consolidations or mergers in the hope that such corrections would lessen the Government's subsidy burden. To encourage such agreements between carriers there must be some incentive, and in many instances this incentive must be something stronger than a mere desire to expand, or to dispose of a marginal route or service. This fact, too, has been recognized by the Board, and the very decision approving the purchase price involved in the sale of Route No. 68 was based in very large measure upon the Board's desire to encourage such agreements between carriers by permitting the realization of a reasonable profit. In its opinion the Board said:

3545 "It is a fact of common experience in utility regulation, which has been recognized by the Interstate Commerce Commission, that the property and business of a successful utility have considerable value and will not be sold to another unless the purchaser pays more than the net depreciated value of the tangible assets. If successful air carrier properties are not recognized by this Board as having a market value which is somewhat in excess of the investment value of the properties for rate-making purposes, the possessor of such properties will have no incentive to transfer such properties to another air carrier who would be in a position to operate them with greater advantage to the public interest. In view of the interest which this Board has shown in the improvement of the air pattern of the Nation wherever such improvement is found necessary to the economic strengthening of an air carrier and the furtherance of the public convenience—an interest which is attested by several pending investigations looking toward possible improvements in the air pattern—it would

*be strange indeed if the Board were now to declare a policy of hostility to any commercial profit however reasonable in any exchange transactions when the certain result would be substantially to 'freeze' the air pattern of the Nation to its present design and thereby thwart one of the very purposes which the Board has expressed an intention to promote."*¹ (Italics supplied)

The present decision in effect reverses the policy thus expressed. The "commercial profit" which accrued to Western as a result of the transaction now turns out to have been an illusory one, since it is to be offset against mail pay, and thus denied to the carrier as effectively as though it had never been allowed in the first place.

Aside from the element of unfairness to the carrier inherent in this shift of position, I firmly believe that the importance of strengthening the national air pattern demands that we offer every reasonable encouragement to the carriers to explore voluntary route adjustments and to present them to the Board. I fear that the present 3546 decision will have an opposite effect, and will result in that "freezing" of the present route system which the Board has previously felt it important to attempt to guard against.

In all other respects, I concur with the majority.

S/ HAROLD A. JONES

¹ United-Western, Acquisition of Air Carrier Property, 8 C.A.B. 298, 323 (1947).

3547

Orders Serial Number E-4870

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 24TH DAY OF NOVEMBER, 1950

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of
mail by aircraft, the facilities used and useful therefor,
and the services connected therewith, of
INLAND AIR LINES, INC.

over its entire system, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar
as authorized under its certificates for interstate transpor-
tation and over its routes between the United States and
terminal points in Canada.

**Order Fixing and Determining the Fair and Reasonable Final
Rates of Compensation For the Transportation of Mail
by Aircraft**

Public hearing having been held in the above-entitled
consolidated proceeding for the determination of the fair
and reasonable mail rates for both Western Air Lines, Inc.,
and Inland Air Lines, Inc., for periods prior to January
1, 1949;

The Board, upon consideration of the record, having
issued an opinion containing its findings, conclusions, and
decision in this consolidated proceeding, which is attached
hereto, and made a part hereof;

IT IS ORDERED, That the fair and reasonable final rate of
compensation to be paid Western Air Lines, Inc., for the
transportation of mail by aircraft, the facilities used and
useful therefor, and the services connected therewith, over

its routes within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada, for the period May 1, 1944-December 31, 1948, inclusive, is hereby fixed, determined, and published to be the amount of \$3,580,526.

3548 IT IS FURTHER ORDERED, That the fair and reasonable final rate of compensation to be paid Inland Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its entire system for the period March 28, 1947-December 31, 1948, inclusive, is hereby fixed, determined, and published to be the amount of \$1,022,793.

IT IS FURTHER ORDERED, That the compensation ordered herein shall be in lieu of the mail compensation heretofore received by each carrier, respectively, for mail transported during the periods specified above.

IT IS FURTHER ORDERED, That this order fixing the fair and reasonable final mail rate for each carrier will be stayed for a period of 10 days from the date of service thereof. If no exceptions are filed hereto within such period, the order will become effective. If exceptions are so filed, the order will be stayed pending disposition by the Board of such exceptions.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN
M. C. MULLIGAN
Secretary

(SEAL)

* * * * *

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| Year 1948 | | | | 36 Month Period | | | |
|-----------|----------------|----------------|-------------|-----------------|----------------|-------------|----------------|
| | As Adjusted | As Reported | Adjustments | As Adjusted | As Reported | Adjustments | As Adjusted |
| | \$ 8,636 | \$6,250 | - | \$6,250 | \$31,251 | - | \$31,251 |
| | 146 | 103 | - | 103 | 623 | - | 623 |
| | 120 | 165 | - | 165 | 344 | - | 344 |
| | 70 | 51 | - | 51 | 264 | - | 264 |
| | 269 | 147 | \$-14 | 134 | 938 | \$ -172 A,E | 766 |
| | \$ 9,241 | \$6,716 | \$-14 | \$6,702 | \$33,420 | \$ -172 | \$33,248 |
| | \$ 1,963 | \$1,983 | \$-23 C | \$1,960 | \$ 7,097 | \$ -1 C | \$ 7,696 |
| | 1,427 | 650 | 273 D | 923 | 4,949 | -475 D | 4,494 |
| | 1,194 | 865 | 105 E | 970 | 4,008 | -745 E | 3,263 |
| | \$ 4,584 | \$3,498 | \$355 | \$3,853 | \$16,654 | \$-1,221 | \$15,433 |
| | \$ 1,579 | \$1,294 | - | \$1,294 | \$ 5,968 | \$ -85 F | \$ 5,883 |
| | 780 | 528 | - | 528 | 2,779 | -159 G | 2,620 |
| | 764 | 656 | -20 H | 636 | 3,026 | -62 H | 2,964 |
| | 1,206 | 1,038 | -36 I | 1,002 | 4,508 | -84 I | 4,424 |
| | 327 | 263 | -8 J | 255 | 1,333 | -37 J | 1,296 |
| | 861 | 761 | -69 K | 692 | 3,579 | -233 K | 3,346 |
| | 154 | 216 | -2 L | 214 | 561 | -2 L | 559 |
| | \$ 5,673 | \$4,756 | \$-135 | \$4,621 | \$21,754 | \$ -662 | \$21,092 |
| | 23 | 8 | - | 8 | 8 | 47 M | 55 |
| | 8 | 2 | 6 N | 8 | 2 | 31 N | 33 |
| | -4 | - | -6 O | -6 | - | -24 O | -24 |
| | \$10,284 | \$8,264 | \$ 234 | \$8,484 | \$38,418 | \$-1,829 | \$36,589 |
| | \$ 1,043 | \$1,548 | \$ 234 | \$1,782 | \$ 4,998 | \$-1,657 | \$ 3,341 |
| | -87 | - | 64 P | 64 | - | -155 P | -155 |
| | -1,099 | - | - | - | - | -1,099 Q | -1,099 |
| | \$ -143 | \$1,548 | \$ 298 | \$1,846 | \$ 4,998 | \$-2,911 | \$ 2,087 |

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Operating Results for the Period April 1, 1947—December 31, 1948¹ as Reported and as Adjusted

(In Thousands)

| | Last 9 Months—1947 As Re- ported | As Ad- justed | Year 1948 Adjust- ments | As Ad- justed | Twenty-One Month Period As Re- ported | Adjust- ments | As Ad- justed |
|---|--|------------------|-------------------------------|------------------|---|------------------|------------------|
| Nonmail Revenues | | | | | | | |
| Passenger | \$1,265 | \$1,265 | — | \$1,564 | \$2,829 | — | \$2,829 |
| Express | 13 | 13 | — | 20 | 33 | — | 33 |
| Freight | 7 | 7 | — | 21 | 28 | — | 28 |
| Excess Baggage | 10 | 10 | — | 13 | 23 | — | 23 |
| Other | 5 | 5 | — | 2 | 7 | — | 7 |
| Total Nonmail Revenue | \$1,300 | \$1,300 | — | \$1,620 | \$2,920 | — | \$2,920 |
| Operating Expenses | | | | | | | |
| Flying Operations | \$ 419 | \$ 419 | — | \$ 630 | \$1,049 | — | \$1,049 |
| Direct Maintenance—Flight Equipment | 214 | A 214 | — | 181 | 252 | \$ 71 A | 466 |
| Depreciation—Flight Equipment | 152 | B 80 | — | 37 | 95 | —14 B | 175 |
| Total Aircraft Operating Expenses | \$ 785 | \$ 713 | \$ -72 | \$ 848 | \$ 97 | \$ 57 | \$1,690 |
| Ground Operations | \$ 339 | \$ 339 | — | \$ 447 | \$ 786 | — | \$ 786 |
| Ground and Indirect Maintenance | 82 | 87 | 5 C | 138 | 220 | \$ 5 C | 225 |
| Passenger Service | 108 | 108 | — | 156 | 264 | — | 264 |
| Traffic and Sales | 133 | 133 | — | 164 | 297 | — | 297 |
| Advertising and Publicity | 49 | 49 | — | 66 | 115 | — | 115 |
| General and Administrative | 112 | 128 | 16 D | 207 | 338 | —3 D | 335 |
| Depreciation—Ground Equipment | 19 | 19 | — | 45 | 64 | 2 E | 66 |
| Total Ground and Indirect Expenses | \$ 842 | \$ 863 | \$ 21 | \$1,242 | \$1,225 | \$ 4 | \$2,088 |
| Total Operating Expense | \$1,627 | \$1,576 | \$ -51 | \$2,090 | \$2,202 | \$ 61 | \$3,778 |
| Break-Even Need | \$ 327 | \$ 276 | \$ -51 | \$ 470 | \$ 582 | \$ 61 | \$ 858 |

¹ Omits last four days of March, which are included in rate period, for practical purposes in working computation. The need for these four days has been estimated at \$6,000, approximately equal to the mail pay received. This amount is not in dispute.

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APPENDIX No. 2 (Page 2)

INLAND AIR LINES, INC.

Explanatory Notes

To Operating Results for Period April 1, 1947—December 31, 1948

| | Last Nine Months 1947 | Year 1948 | 21-Month Period |
|--|-----------------------------|--------------|--------------------|
| A. Adjustment of costs relating to period prior to date of Inland's petition: | | | |
| Labor—Aircraft | \$—10,009 | — | \$—10,009 |
| Reserve Provision—Aircraft | 16,500 | — | 16,500 |
| Actual aircraft overhaul expenses to be capitalized | —21,765 | \$ —8,057 | —29,822 |
| Adjustment of reserve provisions for aircraft and engine overhauls: | | | |
| Aircraft | —16,960 | 15,202 | —1,758 |
| Engines | —36,947 | 42,766 | 5,819 |
| Inland's allocated share of amortization of aircraft overhauls: | | | |
| Built-in overhaul | 2,376 | 766 | 3,142 |
| Actual overhaul | 14,847 | 20,385 | 35,232 |
| Inland's allocated share of routine maintenance expense | 51,905 | — | 51,905 |
| | \$ —53 | \$ 71,062 | \$ 71,009 |
| B. Adjusted depreciation on Western's DC-3 equipment allocated to Inland: | | | |
| Extension of DC-3 service life by spreading book value at May 1, 1944 to June 30, 1949 | \$—56,267 | \$ 57,760 | \$ 1,493 |
| Net adjustment of depreciation on nonrotatable spare parts after crediting provision for loss on retirement | —9,323 | 3,605 | —5,718 |
| Decrease due to elimination of value of built-in overhaul from depreciable cost of aircraft | —6,656 | —3,593 | —10,249 |
| Total | \$—72,246 | \$—57,772 | \$—14,474 |
| C. Allocated portion of cost of Western's move to Los Angeles Municipal Airport | \$ 4,849 | — | \$ 4,849 |
| D. Adjustment of expense allocated from Western to reflect revision in Western's expense level. Tentative Statement showed an increase of \$17,848 in 4th quarter of 1947 and \$68,000 in 1948. The reduction of reported expenses in 1948 is primarily due to an over-allocation from Western to Inland, based on an allowable prorate of 23% of the total recognized general and administrative expenses of the two carriers | \$ 16,454 | \$—18,960 | \$ —2,506 |
| E. Increase in allocated depreciation to reflect allocation of investment in Los Angeles hangar | \$ 429 | \$ 1,718 | \$ 2,147 |

Note: Minus sign (—) denotes deduction. Amounts not so marked are additions.

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APPENDIX No. 3

WESTERN AIR LINES, INC.

*Net Profit From Sale of Route 68 Included as
"Other Revenue"*

| | | | |
|---|----|-----------|-------------|
| Sale price of Route 68 | | | \$3,750,000 |
| Less: Tangible property sold | | | 1,528,478 |
| | | | <hr/> |
| | | | \$2,221,522 |
| Less: Charges by Western against profit | | | |
| DC-6 cancellation charges | \$ | 65,216 | |
| Miscellaneous charges relating to sale | | 32,389 | 97,605 |
| | | <hr/> | <hr/> |
| Net profit before offsets of expense | | | \$2,123,917 |
| Offsets to Profit for Rate-Making Purposes | | | |
| Preoperating and training expense capitalized | | \$114,094 | |
| Extension and development expense capitalized | | 15,394 | |
| Depreciation on flight training equipment | | 52,523 | |
| Abnormal maintenance expense related to Route 68 | | 283,000 | |
| Abnormal loss estimated on retirement of DC-4 non-rotatable spare parts | | 104,000 | |
| Divestment costs | | | |
| Ground operations expense | \$ | 70,000 | |
| Merchandising expense | | 154,000 | |
| General and administrative expense | | 161,175 | 385,175 |
| Loss on engine overhaul equipment | | | 69,745 |
| Loss on Denver reservations system | | | 856 |
| | | <hr/> | <hr/> |
| Total offsets to profit | | | 1,024,787 |
| | | | <hr/> |
| Net profit considered "other revenue" | | | 1,099,130 |

WESTERN AIR LINES, INC.

*Comparative DC-3 Maintenance Expense Per Total Hour
Western and Six Intermediate Carriers*

| Year | Braniff (1) | Capital (2) | Chicago & Conti- Southern (3) | Delta (5) | Mid-Con- tinent (6) | Arith- metic Average (7) | Western (8) | Excess of WAL (8)-(7) (9) |
|-------------------------------|----------------|----------------|-------------------------------------|--------------|---------------------------|-----------------------------------|----------------|------------------------------------|
| 1944 | | | | | | | | |
| Direct maintenance | \$11.13 | \$15.77 | \$13.16 | \$ 3.32 | \$12.12 | \$13.05 ¹ | \$16.03 | \$ 2.98 |
| Ground & indirect maintenance | 10.69 | 12.33 | 11.58 | 6.14 | 5.75 | 10.09 ¹ | 12.06 | 1.97 |
| Total | \$21.82 | \$28.10 | \$24.74 | \$ 9.46 | \$17.87 | \$23.14 ¹ | \$28.09 | \$ 4.95 |
| 1945 | | | | | | | | |
| Direct maintenance | 12.61 | 11.30 | 13.17 | 11.36 | 10.52 | 12.20 | 18.41 | 6.21 |
| Ground & indirect maintenance | 9.65 | 9.11 | 8.35 | 8.62 | 6.30 | 8.79 | 11.64 | 2.85 |
| Total | \$22.26 | \$20.41 | \$21.52 | \$19.98 | \$16.82 | \$20.99 | \$30.05 | \$ 9.06 ² |
| 1946 | | | | | | | | |
| Direct maintenance | 16.85 | 12.29 | 13.60 | 10.99 | 15.27 | 13.12 | 24.74 | 11.05 |
| Ground & indirect maintenance | 9.53 | 8.86 | 7.76 | 11.27 | 8.99 | 9.18 | 14.28 | 5.10 |
| Total | \$26.38 | \$21.15 | \$21.36 | \$22.26 | \$24.26 | \$21.81 | \$39.02 | \$16.15 |
| 1947 | | | | | | | | |
| Direct maintenance | 11.55 | 15.32 | 14.23 | 9.61 | 15.51 | 10.88 | 21.48 | 8.63 |
| Ground & indirect maintenance | 9.22 | 8.88 | 12.34 | 12.75 | 9.86 | 8.34 | 14.98 | 4.75 |
| Total | \$20.77 | \$24.20 | \$26.57 | \$22.36 | \$25.37 | \$23.08 | \$36.46 | \$13.38 |
| 1948 | | | | | | | | |
| Direct maintenance | 14.17 | 13.14 | 15.79 | 9.08 | 13.90 | 11.62 | 16.78 | 3.83 |
| Ground & indirect maintenance | 9.36 | 7.89 | 10.19 | 11.61 | 9.27 | 9.46 | 9.87 | .41 |
| Total | \$23.53 | \$21.03 | \$25.98 | \$20.69 | \$23.17 | \$22.41 | \$26.65 | \$ 4.24 |

¹ Excludes Continental and Mid-Continent, whose DC-3 operations were negligible in 1944.

² Excess before allocation of \$2.00 per hour to DC-4 aircraft (see text).

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WESTERN AIR LINES, INC.

Computation of Western's DC-3 Adjusted Hourly Direct Maintenance Expense

| | 1944 | 1945 | 1946 | 1947 | 1948 |
|---|-----------|-----------|-----------|-----------|-----------|
| Reported direct maintenance expense | \$360,172 | \$739,146 | \$979,006 | \$508,178 | \$291,868 |
| Overhaul Adjustments | | | | | |
| Eliminations | | | | | |
| Actual aircraft overhaul expenses | 7,077 | 70,998 | 65,928 | 33,197 | 11,739 |
| Reserve provisions: | | | | | |
| Aircraft | 12,536 | 25,195 | 40,164 | —10,535 | —20,213 |
| Engines | 40,889 | 20,933 | —29,558 | —24,134 | —55,671 |
| Allocation to Inland of overhaul expenses | — | — | 36,253 | 61,952 | — |
| Allowances | | | | | |
| Amortization of actual aircraft overhauls | 10,001 | 23,610 | 31,151 | 30,483 | 32,537 |
| Adjusted direct maintenance expense | \$309,671 | \$645,630 | \$897,370 | \$478,181 | \$388,550 |
| Total hours | 19,322 | 35,067 | 36,265 | 22,257 | 23,151 |
| Adjusted unit cost | \$ 16.03 | \$ 18.41 | \$ 24.74 | \$ 21.48 | \$ 16.78 |

* * * * *

246.

| | <u>1946</u> | | <u>1948</u> |
|-----|-----------------|-------------------|-----------------------------------|
| | <u>Reported</u> | <u>Recognized</u> | <u>Reported</u> <u>Recognized</u> |
| Net | 1,681 | \$ 205 A | \$-3,644 498 A |
| Inv | 1,199 | 5 | 1,444 9 |
| Ops | 4,534 | 4,303 | 7,235,199 B |
| Non | 23 | - | 10 - |
| Pre | - | 112 C | 49 C |
| Ext | - | <u>31 D</u> | <u>17</u> |
| | 1,075 | \$4,656 | \$5,145,772 |

Ex:

| | | |
|----|-----------|------------|
| A. | 206 | 435 |
| | - | 85 |
| | - | -122 |
| | 1,652 | 227 |
| | <u>28</u> | <u>-68</u> |
| | \$1,886 | <u>557</u> |

B.

| | |
|---|--------------|
| - | 3,135 |
| - | 5,000 |
| - | 5,000 |
| - | 3,712 |
| - | 2,718 |
| - | 3,000 |
| - | 1,000 |
| - | <u>5,000</u> |
| - | <u>5,295</u> |

C.

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3558

APPENDIX No. 6

INLAND AIR LINES, INC.

*Average Reported and Recognized Investment For the
Period April 1, 1947—December 31, 1948
(In Thousands)*

Average for April-December
1947

| | Reported | Adjust- ment | Recogn- ized | Average for the Year 1948 Reported | Adjust- ment | Recogn- ized |
|--|----------|-----------------|-----------------|---------------------------------------|-----------------|-----------------|
| Working Capital: | | | | | | |
| Current assets | \$582 | | | \$430 | | |
| Prepayments and other de- ferred charges | 41 | | | 50 | | |
| Total | 623 | | | 480 | | |
| Current liabilities | 453 | | | 288 | | |
| Deferred credits | 32 | | | 58 | | |
| Total | 485 | | | 346 | | |
| Net Working Capital | \$138 | \$—35 A | \$103 | \$134 | \$—4 A | \$130 |
| Investments and special funds | 4 | —1 B | 3 | 4 | —1 B | 3 |
| Flight equipment (net) | 36 | 227 C | 263 | 16 | 149 C | 165 |
| Ground equipment (net) | 48 | 428 D | 476 | 51 | 556 D | 607 |
| Nonoperating property and equipment (net) | 1 | —1 E | — | — | — | — |
| Intangibles | 108 | —108 F | — | 108 | —108 F | — |
| Total Investment | \$335 | \$510 | \$845 | \$313 | \$592 | \$905 |
| * * * | * | * | * | * | * | * |

3558A

INLAND AIR LINES, INC.

*Average Reported and Recognized Investment For the
Period April 1, 1947—December 31, 1948
(In Thousands)*

Explanation of Adjustments to Investment

| | Apr.-Dec. 1947 | Year 1948 |
|--|-------------------|--------------|
| A. Amount resulting from allocation of working capital between Western and Inland | —7,000 | 67,700 |
| Effect in working capital of reduction in mail pay | —28,264 | —90,791 |
| Elimination of deferred credit offsetting preferred stock retirement fund | 334 | 334 |
| Decrease in accrued tax liability from 69,500 to 51,063 | — | 18,437 |
| | <hr/> —34,930 | <hr/> —4,320 |
| B. Funds for preferred stock retirement | —334 | —334 |
| C. Transfer from Western of investment in DC-3 equipment used by Inland | 236,977 | 149,208 |
| D. Allocated portion of Western's investment in Los Angeles hangar averaged from July 1, 1947 | 427,657 | 555,836 |
| E. Property not used and useful in certificated operations | —501 | —87 |
| F. Contracts and leases originating in recapitalization in 1934 and loss prior to air mail operation | —108,557 | —108,557 |

| <u>OPE</u> | <u>1946</u> | <u>1947</u> | <u>1948</u> | <u>Total</u> |
|--------------|-------------------|-------------------|-------------------|---------------------|
| <u>Fly</u> | | | | |
| | \$ 992 | \$ 1,464 | - | \$ 2,456 |
| <u>Dir</u> | | | | |
| | 115,494 | 40,266 | = | 155,760 |
| | 2,366 | 1,463 | = | 3,829 |
| | \$ <u>117,860</u> | \$ <u>41,729</u> | - | \$ <u>159,589</u> |
| <u>Depr</u> | | | | |
| I | - | - | \$ 7,883 | \$ 21,341 |
| I | - | - | 61,672 | 61,672 |
| I | \$ <u>6,745</u> | \$ <u>7,351</u> | - | <u>14,096</u> |
| | \$ <u>6,745</u> | \$ <u>7,351</u> | \$ <u>69,555</u> | \$ <u>97,109</u> |
| <u>Grou</u> | | | | |
| R | \$ 50,234 | \$ 25,652 | - | \$ 75,886 |
| <u>Adve</u> | | | | |
| C | 6,000 | - | - | 8,000 |
| <u>Gene</u> | | | | |
| C | 9,000 | 14,000 | - | 43,000 |
| | \$ <u>190,831</u> | \$ <u>90,196</u> | \$ <u>69,555</u> | \$ <u>386,040</u> |
| <u>NONOI</u> | | | | |
| Nonoi | \$ 530 | \$ 7,744 | \$ 5,585 | \$ 15,593 |
| Exter | 72,256 | 7,003 | -8,265 | 154,659 |
| Inter | 65,037 | 108,892 | 182,291 | 373,557 |
| Other | 75,301 | 82,451 | 42,902 | 209,240 |
| | \$ <u>213,124</u> | \$ <u>206,090</u> | \$ <u>222,513</u> | \$ <u>753,049</u> |
| <u>Total</u> | \$ <u>403,955</u> | \$ <u>296,286</u> | \$ <u>292,068</u> | \$ <u>1,139,089</u> |
| <u>Const</u> | <u>325,920</u> | <u>403,200</u> | <u>404,040</u> | <u>1,358,840</u> |
| <u>Const</u> | \$ <u>-78,035</u> | \$ <u>106,914</u> | \$ <u>111,972</u> | \$ <u>219,751</u> |
| <u>Const</u> | | | | \$ <u>354,437</u> |
| <u>Const</u> | | | | \$ <u>134,686</u> |

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APPENDIX No. 8

INLAND AIR LINES, INC.

*Computation of Provision For Federal Income Tax on
Constructive Profit*

| | Last Nine Months 1947 | 1948 | 21-Month Period |
|---|-----------------------------|----------|--------------------|
| Expenses Deductible For Tax Purposes Not Recognized For Rate Purposes | | | |
| Excess general and administrative expense | — | \$18,960 | \$ 18,960 |
| Nonoperating property profits or losses | \$ 801 | 75 | 876 |
| Interest expense | — | 1,245 | 1,245 |
| Other nonoperating expenses | 3,054 | 281 | 3,335 |
| Total expense deductions | \$ 3,855 | \$20,561 | \$ 24,416 |
| Constructive profit margin (7% return on recognized investment—Appendix No. 7) | 44,426 | 63,304 | 107,849 |
| Constructive profit margin for tax computation | \$40,571 | \$42,743 | \$ 83,433 |
| Constructive taxable profit | | | \$134,569 |
| Constructive federal income tax | | | \$ 51,063 |
| * * * * * | | | * |

3569

BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.
over its entire system, and of

WESTERN AIR LINES, INC.
over its routes within the continental United States insofar as authorized under its certificates for interstate transportation and over its routes between the United States and terminal points in Canada.

**Exceptions of the Postmaster General to the Final Order (E-4870)
and Accompanying Opinion Issued November 24, 1950,
in the Above-Cited Proceeding**

The Postmaster General, pursuant to the below-mentioned Order and to the subsequent grant of extended time for filing, hereby excepts to the findings of fact and conclusions of law contained in the Opinion and in the accompanying Order, Serial No. E-4870, issued November 24, 1950, in this proceeding, in the following respects:

EXCEPTIONS

I. The final rates of mail compensation fixed and ordered to be paid Western Air Lines, Inc., in the amount of \$3,580,526, and to Inland Air Lines, Inc., in the amount of \$1,022,793, as set forth at page 50 in the Opinion and in the Order itself are in excess of a fair and reasonable rate for each carrier.

A. The final rate for Western is excessive because the Board is permitting excessive expenses of Western to be offset against the profit obtained from the sale of Route 68; these expenses should be disallowed outright.

3570 These expenses which are being treated as offsets are set forth and discussed at pages 33-42 of the Opinion. The arguments against the proposed allowances are fully set forth in the Department's Brief, at pages 25 through 62, and are highlighted in the Department's oral argument before the Board; these arguments are reasserted in support of this exception without being set forth at length herein.

B. The final rates are also excessive for both carriers because of an allowance for taxes in each rate, in the case of Western in the amount of \$134,686, and in the case of Inland in the amount of \$51,063.

The rates now proposed by the Board are set forth in this latest Order. These rates include allowance for taxes. The proposed tax allowances have no relationship to and are excessive when compared with the actual tax liability of each carrier, and thus the tax allowances are excepted to as being unreasonable.

* * * * *

3583

UNITED STATES OF AMERICA
BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of
INLAND AIR LINES, INC.

Over Its Entire System, and of
WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Exceptions to Order Serial No. E-4870 of the Civil Aeronautics Board and Brief of Western Air Lines, Inc. and Inland Air Lines, Inc. in Support of Exceptions.

Western Air Lines, Inc., and Inland Air Lines, Inc. (hereinafter referred to as "Western"), hereby take exception to the Board's Opinion and Order Serial No. E-4870 adopted November 24, 1950, in the above-entitled proceeding.

I.

SPECIFICATION OF ERRORS.

1. The Board erred in finding that the profit from the sale of Route 68 is "other revenue" within the meaning of Section 406(b) of the Act.

2. The Board erred in finding that the profit from the operation of restaurants, concessions and slot machines is "other revenue" within the meaning of Section 406(b) of the Act.

3. The Board erred in finding that the allowance for federal income taxes should not be calculated on the con-

3584 structive basis in accordance with the practice followed by the Board in the Statements of Tentative Findings and Conclusions adopted December 30, 1948.

4. The Board erred in finding that the period for which mail rates shall be established for Western shall be from May 1, 1944 to December 31, 1948.

5. The Board erred in not finding that the mail rates for Western should not be reviewed for the period prior to January 1, 1946.

6. The Board erred in finding that the profits realized and the service rate mail compensation received by Western in 1944 and 1945 should be offset against its mail pay requirements for 1946, 1947 and 1948.

7. The Board erred in assuming that Western is a subsidy need rate carrier for the period under review.

8. The Board erred in finding that the profit realized by Western in 1944 and 1945 while on a service rate should be recaptured, notwithstanding the Board's failure to find that Western earned or realized excessive profits in 1944 and 1945.

• • • • • • • • • •

3815

Orders Serial Number E-5467

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 26TH DAY OF JUNE, 1951

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, of

INLAND AIR LINES, INC.
over its entire system, and of
WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Opinion and Order Disposing of Exceptions.

On November 24, 1950, the Board issued its tentative decision and order ¹ fixing rates of compensation for the transportation of mail by Western Air Lines, Inc. (hereinafter called Western), and Inland Air Lines, Inc. (hereinafter called Inland). Rates were fixed for Western for the period May 1, 1944, through December 31, 1948, and for Inland for the period March 28, 1947, through December 31, 1948. The carriers filed exceptions on January 24, 1951, staying the tentative decision and order, and requested oral argument on the exceptions. The Postmaster General filed exceptions to the tentative decision on January 22, 1951. Subsequently, on February 23, 1951, the Air Transport Association of America, was given leave by the Board to file a brief as *amicus curiae*.² In its request for leave

¹ Order Serial No. E-4870.

² Order Serial No. E-5146.

to file a brief as *amicus curiae*, the ATA had also requested oral argument. All the parties participated in the oral argument on the exceptions held by the Board on May 21, 1951.

The carriers have contended that the Board erred in finding that the profit from the sale of Route No. 68 and from the operation of restaurants, concessions, and slot machines is "other revenue" within the meaning of section 406(b) of the Act; that the allowance for Federal income taxes should be calculated on the constructive basis proposed in the Statements of Tentative Findings and Conclusions adopted by the Board in this proceeding on December 30, 1948,³ rather than the hybrid method used in the tentative decision; and that the period for which mail rates should be established for Western is January 1, 1946, through December 31, 1948, rather than May 1, 1944, through December 31, 1948. The ATA has supported the carriers' objections to the Board's findings regarding the treatment of the profit from the sale of Route No. 68 and the proper allowance for Federal income taxes.

The Postmaster General has also excepted to the tax allowance made in the tentative decision, but, as distinguished from Western and Inland, on the ground that the proper allowance should be determined by the actual tax liability of the carrier. In addition, the Postmaster General has
3817 excepted to the Board's finding that certain costs connected with the promotion, maintenance and sale of Route No. 68 should be offset against the profit from the sale of the route.

We have carefully reviewed the entire record in the light of the specific exceptions of the parties. As a result of our review, we believe, as we explain below, that Western's exceptions regarding the treatment of the profit from the sale of Route No. 68 as "other revenue" should be sustained in part, and that the Postmaster General's exceptions regarding provision for Federal income taxes should also be sustained. However, the other exceptions should be overruled for the reasons discussed below.

³ Orders Serial Nos. E-2333 and E-2334.

Profit from the Sale of Route No. 68

In our tentative decision we found that Western had realized a net profit of \$1,099,000 from the sale of Route No. 68, and that this amount should be deducted from the carrier's mail pay "need" as "other revenue" within the meaning of Section 406(b). The carrier has objected to this finding on grounds of both law and policy.

One of the legal contentions not previously made by the carrier is that Congress did not intend the meaning we have attributed to the "all other revenue" provision of the Act. While conceding that the legislative history of the Civil Aeronautics Act itself does not provide any clue to the meaning of the phrase "all other revenue", Western contends that this phrase is based on Section 6(e) of the Air Mail Act of 1934, and on the Railway Mail Pay Act of 1916. It also contends that since Congress considered the ICC decisions interpreting Section 6(e) before enacting the Civil Aeronautics Act, it must have intended that the language it borrowed from Section 6(e) for inclusion in section 406(b) would be interpreted the way the ICC has interpreted it.

While it is true that the legislative history of the Civil Aeronautics Act contains scattered statements that section 406(b) is based upon the Air Mail Act of 1934 and the Railway Mail Pay Act of 1916, the language and purpose of these Acts are so different from those of the Civil Aeronautics Act that they cannot be considered to control the interpretation of section 406(b). Thus, in the case of the railroads there has been no intent by Congress to provide subsidy in the form of mail payments. As distinguished from the Civil Aeronautics Act, which looks to the "need" of the carrier, the Air Mail Act of 1934 was designed to provide compensation for the transportation of mail on a route basis only.^{3a} In addition, while the 1934 Act contained authority for the fixing of mail rates, it did not provide for the regulation of

^{3a} See *Chicago and Southern Air Lines, Inc., Mail Rates for Route No. 8 and 53*, 3 C.A.B. 161, 189 (1941).

passenger or property rates. In view of these, as well as other, significant differences between the Civil Aeronautics Act and the statutes referred to by Western, it seems clear that any ICC decisions construing the phrase "revenue and profits from all sources" as used in Section 6(e) of the Air Mail Act of 1934 would have no bearing here. In any event, even if they were relevant, we would obviously not be bound to construe section 406(b) in accordance with such decisions.

We are no more persuaded by Western's other major legal contention, namely, that the profit from the sale of Route No. 68 should not be included as "other revenue" because it was derived from a source unrelated to air carrier activity. This argument is substantially the same one Western made prior to our tentative decision. We have already indicated, in our tentative decision, and reaffirm our opinion

that this profit was clearly a part of "all other
3819 revenue" of Western during the period under review.

The language of section 406(b) of the Act can hardly be read otherwise:

"In determining the rate in each case, the Board shall take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

Moreover, we see no distinction for this purpose between the net revenues derived from the sale of tangibles such as operating property and equipment, and the net revenues received from the intangible elements of the sale such as the earning power of the route. Both kinds of revenue originated in the same transaction and augmented the carrier's net income. Both must be considered in relation to the carrier's "need".

While we are required by the Act to "take into consideration" the "need" of the carrier for mail compensation together with "all other revenue", we do not understand the language of section 406(b) as requiring us to reduce the carrier's mail pay "need" with any part of such "other revenue". This is a matter within our discretion. That is, we may take in "other revenue" in whole, in part, or not at all.⁴ However, we will normally use "other revenue"

as available to reduce "need" unless there are exceptional and compelling circumstances which dictate otherwise. In this case, as we shall explain below, we conclude that the developmental objectives of the Act require that the carrier be permitted to retain a part of the profit from the sale of Route No. 68.

Western and the ATA have contended most vigorously that the Board's decision in the *United-Western, Acquisition Air Carrier Property Case*⁵ states very clearly the considerations which must control whether the profit from the sale of Route No. 68 is to be included as "other revenue". Although, as we stated in the tentative decision, the Board was not concerned in that case with the ultimate treatment of the profit which was to be realized by Western, we do agree that the views of the majority in that case must form the keystone of our decision here.

The Board was primarily concerned in the *Acquisition* case with determining whether the transfer of the route at the amount to be paid by United was in the public interest. The Board decided that it would be in the public interest to allow Western to sell its air carrier properties at a profit because it would provide the necessary incentive for Western to dispose of the properties to another carrier which was in a position to operate them with greater advantage

⁴ Cf. *Chicago and Southern Air Lines, Inc., Mail Rates, Latin American Operations, Statement of Tentative Findings and Conclusions*, Docket No. 2564, Order Serial No. E-5385 (May 18, 1951) in which the Board stated that as a matter of policy it would not offset the profits from the domestic division of Chicago and Southern earned under a final rate in establishing the mail rate for the international operation.

⁵ 8 C.A.B. 298 (1947).

to the public. Recognizing its impotence under the Act to compel route transfers, the Board said:

"We know of no direct or indirect means available under the existing law by which an air carrier can be forced against its will to transfer its property, business, and certificate to another air carrier. If such transfers are to be accomplished under the existing law it would seem that the inducement of reasonable market prices, except in rare instances, would be found necessary even though such prices contained sufficient commercial profit to the seller to generate a business incentive to sell. . . .

3821 "We can find no justification for a decision which would outlaw the profit incentive from business transactions like that before us." ^{5a}

It was the Board's serious concern in the *Acquisition* case that unless Western were allowed a "commercial profit" from the then proposed transaction, the Board would be thwarting the improvement of the air pattern through voluntary action by the carriers. Improvement of the national air pattern has been for some time, and still is, a primary objective of the Board. It should be apparent, therefore, that we must consider the possible effect of our action in this proceeding on what the Board was trying to accomplish in the *Acquisition* case. If we now decided to deny Western the right to keep any part of the profit permitted in that case, we would, in effect, override the considerations which prompted the opinion and destroy the possibility of the incentive which the Board found so important. In order to avoid the danger of confining the present air pattern to a rigid mold, and to continue to encourage voluntary action by the carriers, we believe that the incentive of profit which may be derived from the sale of a route so clearly approved in the *Acquisition* case should be preserved here.

We believe we may do so in a manner consistent with our previous decisions. If Western had sold the operating property and equipment involved in the transfer of Route No. 68

^{5a} *Id.* at 323.

without reference to the certificate and the other intangibles, there would have been ample authority for holding that the profit from the sale of the tangible property should have been applied to reduce the amount of the carrier's "need" to be met by mail pay.⁶ In the instant case, however, 3822 the sale transaction included both tangible and intangible elements of value.⁷ While the tangible and intangible elements together made up the single transaction, it does not follow that they are inseparable for the purpose of determining whether, and to what extent, this "other revenue" should be offset against Western's "need". Since we know of no controlling reason why the carrier's need should be duplicated by the net profit from the sale of the tangibles, we find that this amount should be included as "other revenue" in line with the previous cases relating to the treatment of profit from the sale or retirement of operating property and equipment.⁸

On the other hand, if we are to safeguard the incentive for voluntary route transfers, we cannot now refuse Western the right to retain at least some portion of the net profit from the sale of Route No. 68. Therefore, it seems appropriate under the circumstances to allow Western to keep the net profit from the sale of the intangibles, which the Board found to be composed almost entirely of the earning power of the route, because it was the latter factor which played the decisive part in the route transfer.

This appears to be a case of first impression since we have never previously had occasion to decide whether the

⁶ *Continental Air Lines, Inc.*, Mail Rates, Docket No. 3281, Order Serial No. E-4332 (June 21, 1950); *Colonial Airlines, Inc.*, Mail Rates, 4 C.A.B. 71 (1942); *Pennsylvania-Central Airlines, Inc.*, Mail Rates, 4 C.A.B. 22, 30 (1942); *Chicago and Southern Air Lines, Inc.*, Mail Rates, 3 C.A.B. 161 (1941); *Delta Air Corp.*, Mail Rates, 3 C.A.B. 261, 270 (1942).

⁷ With respect to the sale of tangible property, we stated in the tentative decision that the carrier had realized a net profit of \$722,000. However, we agree with Western that an additional \$70,000 of expense representing the carrier's loss on engine overhaul equipment should properly be charged against the profit from the sale of tangible property. As a consequence, we now find that the carrier's net profit from the sale of tangible property was only \$652,000.

⁸ See cases cited *supra* note 6.

3823 profit from the sale of an intangible composed almost exclusively of the earning power of a route should be included as "other revenue". However, it should again be emphasized that our decision not to include the net profit from the sale of intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers. In other words, we have decided not to offset this profit against the carrier's need because we are seeking in this way to spur the development of a self-sufficient air transport industry.

Offsets Against the Profit from Route No. 68

The tentative decision allows Western a total of \$1,122,000 as an offset against the profit from the sale of Route No. 68⁹ because expenses in that amount were found attributable to the establishment, maintenance, and disposition of the route. This finding was in line with the Statement of Tentative Findings and Conclusions on this point. The Postmaster General objected originally to the proposal to allow offsets in the Statement, and excepts to all but \$32,000 of the total amount allowed in the tentative decision.

In view of our decision not to include as "other revenue" Western's net profits from the sale of the intangible elements involved in the transfer of Route No. 68, it is not necessary to determine how much of the price paid for intangible values in the sale of the route was profit to Western, and how much was chargeable as expenses. If allowable at all, any offsets would be permitted as 3824 deductions from the profit received from the sale of the intangibles. Since we have determined that this profit should be left intact with the carrier, we cannot affect

⁹ The Board found in the *United-Western Acquisition of Air Carrier Property Case*, 8 C.A.B. 298 (1947) that the sale price of the intangible elements involved in the transfer of Route No. 68 was \$1,500,000.

it by adjustments through offsets.¹⁰ Accordingly, there is no occasion to consider the Postmaster General's exceptions to the allowance of offsets.

Profits from the Operation of Restaurants, Concessions, and Slot Machines.

We are not aware of any compelling reason which would support Western's request for modification of our previous finding that the profits from restaurants, concessions, and slot machines should be considered "all other revenue" to be applied against Western's total mail pay "need". Western maintains that the profits from these various activities must be excluded from consideration even under the test used in the tentative decision, namely, whether the restaurants, concessions, and slot machines were a separate and distinct operation apart from the air transportation services performed by the carrier. In making this argument, Western seems ready to concede that the profits from its restaurants at Salt Lake City, Las Vegas, and Long Beach may be included as "other revenue", but it insists that the operation of slot machines at Las Vegas which accounted for about 85% of the \$88,000 netted by the carrier from these three sources, was "not necessary nor even a remotely related incident to Western's air carrier activities." As we pointed out in the tentative decision, the lease

for the carrier's air transport operations at Las Vegas clearly demonstrates the close tie-in with

Western's air carrier operations of the various concessions leased by Las Vegas to Western. It covers not only the rental of the facilities required to operate the planes themselves, but a host of other items including the operation of vending, and slot, machines. The clause granting Western the right to terminate the *entire* lease in the event commer-

¹⁰ However, we are satisfied that substantial expenses were incurred in the development, operation, and sale of Route No. 68, and were not the result of inefficient or uneconomical operations.

With respect to the profit on the sale of tangible property we have found that \$70,000 should be charged as a loss on engine overhaul equipment. See *supra* note 7.

cial operations were suspended at the airport is significant of the close tie-in. We cannot recognize Western's claim that the cancellation provision emphasizes the possibility of the U. S. Government's taking over the airport. The lease mentions the possibilities of cancellation by Western and the Government's assuming Western's operations, and states them as alternative possibilities enabling Western to cancel the lease.

In any event, we believe that in addition to the reasons given in the tentative decision for taking in the net profits from restaurants, concessions, and slot machines as "other revenue", we should do so for essentially the same reasons we are applying against Western's "need" the net profit from the sale of tangibles involved in the transfer of Route No. 68. That is, in our opinion, Western's net profit from the operation of restaurants, concessions, and slot machines is undoubtedly part of the carrier's "all other revenue", and we are aware of no consideration which advises against charging this revenue to the carrier's need for mail compensation.

3826 *The Rate Period which should be Fixed
for Western*

Western alone has excepted to our decision to fix rates for the carrier for the period May 1, 1944, when it filed its petition, to December 31, 1948. It argues now, as it has throughout this proceeding, that the rate period should not antedate January 1, 1946, which it has chosen as a convenient cut-off date, but which has no special significance. It relies on substantially the same arguments on this issue that it made in brief and argument prior to the tentative decision. Having thoroughly considered them again, we are no less convinced of our original position as stated in the tentative decision. Accordingly, we overrule the exception, noting only the highlights of Western's supporting arguments.

Western is again contending that its petition in this case was of a limited nature and, therefore, did not give the

Board the right to review its rates generally. Its major point in this connection appears to be that the petition requested an increase in mail rates and did not put in issue the question of whether the carrier was earning excessive amounts of mail pay. In answer to this objection we need only point out again that the carrier has in fact been granted an increase for the entire review period. Besides, it would be a strange doctrine indeed which limited our authority to review rates to an examination of operations showing losses only. Carriers do not usually petition for decreases in rates of mail compensation.¹¹ Moreover, once the rate period is thrown open, whether by petition of the carrier or by 3827 order of the Board, we cannot close our eyes to operating results after the date of initiation of the proceedings depending on whether the data reflect losses or gains.

Western's contention that the Board is allowing the carrier nothing for carrying the mail for the last eight months of 1944, and has substantially reduced the rate otherwise effective in 1945 is without merit. The mail pay which we have proposed for Western for the entire past period satisfies the carrier's break-even need and provides a 7% return on investment for every year beginning May 1, 1944. Consequently, there can be no question of the constitutional, or statutory, adequacy of the mail rate.

Western's other major legal contention is that the Board, in the tentative decision, did not meet the issue of whether Western's profits of 1944 and 1945 were excessive. This argument reveals that Western is under a misapprehension as to the purport of our decision to review the carrier's rates as of May 1, 1944. There is no issue here as to whether the carrier's earnings were excessive, and therefore, we have not even considered such a finding. Our duty, as we have already indicated, is to review the carrier's operations

¹¹ A notable exception to the general practice is the petition of Southwest Airways Co., filed April 24, 1951, Docket No. 4923, which did request a decrease in the carrier's rates of compensation for the transportation of mail.

for the entire period since the rate was thrown open, without regard to whether there have been losses or gains. The carrier itself is injecting the test of gains or losses by its proposal that we adopt a January 1, 1946 cut-off date. The only possible reason for doing so is the fact that prior to this date the carrier earned substantial profits which Western would thus screen off from consideration in connection with the establishment of its mail rate. If we adopted such a proposal, we would have to contend with a shifting frame of reference designed entirely to insure for the carriers a "heads I win, tails you lose" system of rate-making.

It is true, as Western contends, that the non-mail revenues earned during 1944 and 1945 are included for review with those of 1946, 1947, and 1948 and are balanced against expenses during the entire review period so that the existence of substantial profits in 1944 and 1945 decreases the break-even need which otherwise would result for 1946, 1947, and 1948 alone. This fact does not warrant excluding the years 1944 and 1945. From such a premise Western could as well argue that in any given year under review the Board should consider only the months in which losses were incurred, without taking into account those periods of the year in which the carrier showed gains. Obviously, such a position is untenable. Accordingly, we will not isolate from the review period those portions which the carrier is not disposed to have considered.

The plain effect of accepting Western's contentions would be to guarantee to the carrier that its losses would be met without incurring the risks which carriers on final rates must meet. In other words, Western is again asking for a better than cost-plus system of rate-making rather than the normal public utility rate-making pattern which the Supreme Court found to be controlling in the *TWA* case.¹² We have tried to make clear that it is our mail rate policy

¹² *Transcontinental & Western Air, Inc. v. Civil Aeronautics Board*, 336 U.S. 601 (1949).

to discourage the filing of protective petitions. This, as we have pointed out in the tentative decision and in the recent *Braniff*¹³ and *Continental*¹⁴ cases, will be done by making mail rates effective as of the filing date of the carrier's petition, so that profits earned, as well as losses incurred, after the date of the petition are also considered. Aside from the other undesirable features involved in Western's proposal, it would also run counter to our constant efforts to have carriers operating on a future rate basis for as long as possible.

Western is also repeating its argument that even if the Board may legally review the carrier's rates prior to January 1, 1946, it should not do so for reasons of policy and fairness. The carrier says it can see no real distinction between its own situation and that of other carriers which were permitted to retain excessive earnings received during World War II, and insists that it would be an injustice to treat Western differently. As authority for the latter contention it cites again the Board's decisions in the *Pan American-Grace Airways Case*¹⁵ and the *Chicago and Southern Case*.¹⁶

We tried to make clear in our tentative decision that there were important factors distinguishing the *Panagra* case from the instant case. For example, we pointed out that the Board decided not to reduce Panagra's mail pay because of the uncertainties of war time operations as well as the requirements for operating its international routes. As for Western's additional argument that there were other considerations which motivated the Board's decision in the *Panagra* case such as the doubt which would be cast on the carrier's financial position by an order involving the recapture of past earnings "accumulated over a substantial

¹³ *Braniff Airways, Inc.*, Mail Rates, Docket No. 3601, Order Serial No. E-4285 (June 5, 1950).

¹⁴ *Continental Air Lines, Inc.*, Mail Rates, Docket No. 3281, Order Serial No. E-4332 (June 21, 1950).

¹⁵ *Pan American-Grace Airways, Inc.*, Mail Rates, 3 C.A.B. 550 (1942).

¹⁶ *Chicago and Southern Air Lines, Inc.*, Mail Rates, 9 C.A.B. 786 (1948).

period of time,"¹⁷ we are aware that these considerations were noted in that case but we do not regard them as controlling in the instant case. In retrospect it seems clear that the fact of total war and the major role of an international air carrier in that war were the effective determinants of the Board's decision not to reduce *Panagra's* rates retroactively.¹⁸ While we have taken into account the other considerations referred to, we do not believe they are sufficiently persuasive to warrant reducing the rate period.

In any event, nothing in the *Panagra* case supports the split in the past period contended for by Western. In that case the Board considered the question of establishing a final rate for the entire past period in an amount lower than the challenged rate under which the carrier had received payment. That decision did not disturb the challenged rate for any *part* of the past period but made it final for the *entire* review period. The past period was considered as a whole, and for the entire period the carrier and the challenged mail rate were left as they had been as of the date of the initiation of the proceeding.

Moreover, there is no question of recapture of excess profits in this case. The only question is whether Western's mail pay requirements shall be increased by arbitrarily excluding from review the various months when its operations were profitable.

We have also said in our tentative decision that to the extent our decision in the *Chicago and Southern* case is inconsistent with the principle enunciated here as well
3831 as in the *Braniff* and *Continental* cases, we are prepared to overrule the earlier cases. It is well settled

¹⁷*Pan American-Grace Airways, Inc., Mail Rates*, 3 C.A.B. 550, 564 (1942).

¹⁸ Thus, the Board said, in the course of the *Panagra* opinion, "It would be inexcusable error to ignore the economic uncertainties which surround air transport operations in time of war. This conclusion needs no bill of particulars to support it; war developments affecting international air transportation in the Pacific area and elsewhere amply attest to its validity." *Pan American-Grace Airways, Inc., Mail Rates*, 3 C.A.B. 550, 563 (1942).

that agency action which is otherwise proper does not become improper because it may involve the application of a policy different from that previously followed.¹⁹ As we have indicated above, we believe that decisions in this case and in the *Braniff* and *Continental* cases announce the better rule with respect to our responsibility for reviewing a carrier's operations in a mail rate proceeding instituted by its own petition.

The Proper Allowance for Federal Income Taxes

The carriers, supported by the ATA, have objected to the method of providing for income taxes used in the tentative decision. According to this method the constructive profit before taxes, as determined from the allowable return on investment is reduced by the amount of expenses actually incurred by the carrier which are not recognized for mail rate purposes but which are treated as expenses deductible for tax purposes. The application of this method, which we shall refer to as the "hybrid method", a term suggested by the participants in this proceeding, produced a tax allowance of \$134,686 for Western and \$51,000 for Inland. The carriers maintain that we should calculate the tax allowance according to the method customary in past cases. Under the latter completely constructive method, provision for Federal income taxes was made on the assumption that the net taxable income for tax purposes was identical to the profit for rate purposes except for the tax deduction for interest on indebtedness. According to this method, Western's income tax allowance would have been slightly under \$600,000, and Inland's would have been \$71,000.

On the other hand, the Postmaster General has excepted to the hybrid method in favor of the determination of the carriers' actual income tax liability as the basis for the tax allowances. His thesis is that Western's tax returns showed

¹⁹ *F. C. C. v. Pottsville Broadcasting Co.*, 309 U. S. 134 (1940); *Georgia P.S.C. v. U.S.*, 283 U. S. 765, 774 (1931); *Virginia Railway Co. v. U. S.*, 272 U. S. 658, 665 (1926).

no actual tax liability for the period in question.²⁰ At the oral argument Bureau Counsel also took the position that the tax allowances should be computed on the basis of actual tax liability. Thus, the hybrid method, which was not considered in briefs or oral argument by the parties prior to the tentative decision, has found favor with none of the participants in this proceeding.

This appears to be the first case to have come before us in which it has been shown that the customary constructive tax basis would result in awarding the carrier an amount for income taxes which has not been, and will apparently not be, disbursed, and which must, therefore, be considered a windfall to the carrier. The hybrid method we adopted in the tentative decision is open to much the same kind of objection although the amount of the windfall is substantially less. In the tentative decision we pointed out that the "ideal" policy to follow would be to provide for only that amount of income tax for which liability can be determined from analysis of income tax returns. This we will refer to

hereafter as the tax return method.²¹ However, when
3833 we adopted the tentative decision, we decided for reasons of administrative expediency to use the hybrid method which we believed afforded reasonable assurance of producing an approximation of actual tax liability over a substantial period without the practical difficulties complained of by the parties. In adopting herein the tax return method, we are, in effect, reaffirming the basic finding in the tentative decision as to the desirability of providing for actual tax liability only.

Inquiry into the purpose underlying the income tax allowance readily demonstrates why we consider the two con-

²⁰ Of course, this contention was made prior to statements at the oral argument by counsel for Western regarding adjustments of the carrier's taxable income by the Bureau of Internal Revenue. See *infra* note 30.

²¹ By the tax return method in past period mail rate cases we mean the technique of providing for a carrier's liability for income taxes on the basis of reliable evidence regarding the carrier's tax returns filed with the Bureau of Internal Revenue, together with any adjustments made by the Bureau as of the most recent practicable date prior to the Board's order establishing final mail rates.

structive methods unsuitable. Mail rates for domestic carriers for past periods are generally established in amounts which meet the carrier's "need", under honest, economical, and efficient management, and also provide a 7% return on the recognized investment. These two amounts together constitute the fair and reasonable rate of mail compensation required by section 406(b) of the Act. A third amount is also provided to cover Federal income taxes on the theory that if the carrier must pay taxes on the profit included in the mail rate, it will not, in fact, receive the fair and reasonable rate to which it is entitled. Therefore, as we see it, the function of the Federal income tax allowance is to insure that the carrier receives this compensation as if it were a cost of doing business. On the other hand, this allowance is not designed to guarantee that the carrier will receive a gratuity or bonus which it can use to offset other losses. An allowance greater than the actual tax liability affords such a gratuity and should be avoided if possible.

3834 While the purely constructive method is the most simple to administer, it is too crude a technique for reimbursing carriers for their actual Federal income tax expense. Of the three possible methods under consideration, it is the one which invariably affords the largest tax allowance, and the largest windfall.

If we are to avoid a windfall to the carriers through the tax allowance it is clear that we cannot adopt either the constructive or the hybrid methods. We are warned, however, that if we adopt a technique which relies on tax returns we will find ourselves with an impossible task. Thus, we are reminded that tax returns may be subject to audit by the Bureau of Internal Revenue after the date of the final rate order; that certain carriers have non-transport activities; that others operate a number of divisions, etc.; and that it is factors such as these which will prevent effective application of the tax return method. As we have pointed out, at the time we decided to adopt the hybrid method we were largely persuaded to do so by the difficulties we might en-

counter if we attempted to arrive at the Federal income tax allowance by determining tax liability from analysis of income tax returns. We went so far as to say that we did not consider the latter method "feasible"; instead, we expressed confidence that the hybrid method would accomplish substantially the same result in a "relatively simple" way. However, it has not proved to be a simple technique and has furnished the carriers with sizeable windfalls. Consequently, if, in the administration of the hybrid method, we must cope with problems as complex as those we may reasonably expect to have to solve in ascertaining actual tax liability, we believe it preferable to struggle with them armed with the reasonable prospect of avoiding further gratuitous payments to the carriers.

3835 It would serve no purpose at this point to consider separately the problems we are told we will have to face in attempting to compute actual liability, or the various ways we may be able to overcome them. While we expressed serious doubts about the feasibility of the method in the tentative decision, on further examination we believe that these problems will be no more difficult than other situations which often confront us in the complex area of rate-making. Moreover, we now find that the simplicity of the wholly constructive method was enjoyed at too high a price to justify that procedure.

The one substantive argument the carriers made against the application of a method which is designed to establish actual tax liability is that rather than avoiding a windfall to the carrier, such a method "punishes the carrier twice." The carriers' view is that not only does the airline suffer but the usual disallowances of expenses incurred and paid in the course of business but not recognizable for rate-making purposes, it also fails to receive the tax allowance which under the constructive method helps cushion the effect of such disallowances. What Western and Inland are insisting on therefore, is that for every dollar disallowed for rate-making purposes—e.g., an expense incurred because of un-

economic or inefficient management—there must be returned to the carrier an amount representing Federal income taxes on that dollar even though no taxes have been, or will be, paid on the dollar. (There is normally no tax liability because the Bureau of Internal Revenue usually allows the item to be deducted for tax purposes). The constructive method is thus revealed as a convenient vehicle for reimbursing carriers for substantial parts of funds disallowed by the Board in accordance with the rate-making standards of the Act. The carriers characterize the denial of 3836 this kind of reimbursement as “punishing” the carrier. On the contrary, we consider such allowances gratuities which we can no longer tolerate.

In addition to the practical objections made to the hybrid and actual tax methods, the carriers and the ATA assert it would be discriminatory and unfair for the Board in this case to use any method of computing the tax allowance other than the wholly constructive one used in the past. This argument is largely based on the view that the proposed change in the tax policy cannot be made to operate retroactively because it would mean the establishment of a different standard from that used for other carriers in similar situations. We have already had occasion in our discussion of the proper rate period in this proceeding to point out that agency action which is otherwise proper does not become improper because it may involve the application of a new and different policy.²² An administrative agency charged with the protection of the public interest is certainly not precluded from taking appropriate action because of mis-

²² See *supra* page 17, and cases cited note 19. It should be pointed out, however, that as early as July, 1948, the Board recognized that the wholly constructive method of computing the tax allowance required some revision. (*Chicago and Southern Air Lines, Inc. Mail Rates*, 9 C.A.B. 786 (1948)). In this case the allowance was based on the profit shown for rate making purposes reduced by the amount of interest on long-term debt, since interest represents an allowable deduction for tax, but not for rate, purposes. This deviation was, in a sense, the initial step toward the adoption of a method intended to determine actual liability. See also *Capital Airlines, Inc. Mail Rates*, 10 C.A.B. 705 (1949).

taken action on its part in the past.²³ The contention that prior policy must be followed unswervingly to avoid possible discrimination is not supportable.²⁴ Moreover, in this case there is no evidence that the carriers acted in reliance on their alleged assumption that they would receive the customary tax allowance and that they sustained harm as a result.

It is also alleged that it will be discriminatory to use the tax return method because it cannot be applied to the determination of the tax allowance of a prospective mail rate. The argument runs that a carrier with a final rate will continue to receive the full tax allowance even though it participates in activities or incurs expenses which will not be considered in fixing mail rates for another carrier operating pursuant to a temporary rate. Thus, as distinguished from the carrier on a final rate, if the carrier on a temporary rate made a charitable contribution, not only would this expense be disallowed by the Board, but the supposed tax benefit would be lost as well. We cannot overlook the fact that a carrier on a temporary rate is operating on a cost-plus basis. Expenses reasonably incurred will be met by the Board, and the carrier's break-even need will be satisfied. In that situation a "need" carrier can hardly be heard to complain that the Board is denying it an allowance for taxes it will never have to pay. On the other hand, the carrier on a final rate not only has the admitted benefit of the full tax allowance, it also has the burden of meeting out of its own funds all losses it may incur including, for example, those resulting from services not recognized for rate-making purposes.

²³ *NLRB v. Baltimore Transit Co.*, 140 F. (2d) 51, 55 (CCA 4th, 1944), cert. denied, 321 U. S. 795 (1944).

²⁴ See *FCC v. WOKO*, 329 U. S. 223, 228 (1946); *Northern Pacific Ry. Co. v. United States*, 41 F. Supp. 439, 446 (Dist. Ct. D. Minn., 1941); *Churchill Tabernacle v. FCC*, 160 F. (2d) 244, 246 (App. D. C., 1947). While Western has extracted language from the *WOKO* case which appears to lend support to its contention, the Court there actually held that the F.C.C. was not bound to deal with all cases at all times as it had dealt with others that appeared to be comparable.

Western contends that since it had no notice prior to the issuance of the tentative decision that the Board would adopt the hybrid method of computing the allowance for income taxes, it had no opportunity to be heard on certain issues. The carrier's point in this connection is, although it offers no evidence to support its assertion, that at the rate conference which preceded the issuance of the Statement of Tentative Findings and Conclusions in this case it was willing to accept the disallowance of \$479,000 of various expenses—out of a total of \$1,139,000 of cost adjustments—only because the Board's staff stated the Board would follow the usual practice in computing the Federal income tax allowance. It now says it hoped in this way to reach agreement on the ultimate mail rate more quickly, secure in the knowledge that the income tax allowance would provide a "cushion" which would permit it to absorb part of the disallowed expense. Even if this were true, which we are not called upon to decide, it must be pointed out that at the prehearing conference in this proceeding all issues originally agreed upon by the participants in the rate conferences were open pursuant to the usual notice given in the Order to Show Cause²⁵ regarding the effect of the filing of an answer.²⁶ Accordingly, if the carrier actually had had a sound basis for opposing any of the conceded expenses, it could have done so at the prehearing conference upon learning that the other parties to the proceeding were going to take a position against the usual constructive tax method.

3839 We turn now to a consideration of the carriers' tax liability as reflected in their tax returns. All of the mail compensation received by Western for the period May 1, 1944, through December 31, 1948, i.e., \$3,277,000, was reported as gross income in the carrier's Federal income tax

²⁵ Order Serial No. E-2333.

²⁶ The notice stated: "IT IS FURTHER ORDERED, That, if answer is filed hereto, all elements entering into the determination of a fair and reasonable rate, except insofar as limited in prehearing conference, shall be in issue, and in such event the final rate shall be determined upon the record made with respect to all issues stated in the prehearing conference report."

returns filed for the years 1944-1948 inclusive.²⁷ According to these returns, Western incurred no income tax liability for the entire review period.²⁸ On the present record we find that Western will still have no Federal income tax liability for the period in question, even though we are awarding herein final mail compensation of \$3,909,027²⁹ rather than the abovementioned \$3,277,000. Accordingly, in view of our revised policy of providing for taxes as discussed above, we shall not make any allowance for Federal income taxes in the rate of mail compensation established for Western herein.³⁰

²⁷ Additional temporary mail pay of \$975,000 was awarded Western for the past period in our temporary rate order of February 25, 1949 (Order Serial No. E-2506). To the extent allowed as final mail pay, such additional mail compensation would, of course, be additional income for the years 1944-1948.

²⁸ While the carrier's returns were not introduced in evidence, pertinent portions were analyzed in Public Counsel's exhibits and in the course of testimony by Western's treasurer. Thus, the record shows that an income tax liability was incurred in 1944, 1945, and 1947, but that this liability was wiped out by the carry-back of losses for tax purposes in 1946 and 1948.

²⁹ The amount of mail pay to be fixed for Western herein in addition to that awarded in the tentative decision is computed as follows:

| | |
|---|-------------|
| Amount offset against need in tentative decision (total net profit from sale of Route No. 68) | \$1,099,000 |
| Revised amount offset in the opinion herein (net profit from sale of tangible property, explained <i>supra</i> note 7) | 652,000 |
| | <hr/> |
| This increases break-even need | 447,000 |
| Increase in return to reflect inclusion of additional mail pay in recognized investment | 16,187 |
| | <hr/> |
| | 463,187 |
| Eliminate provision for taxes under the hybrid method used in tentative decision | 134,686 |
| | <hr/> |
| Additional mail pay over amount allowed in tentative decision | \$ 328,501 |

³⁰ In the oral argument on the exceptions, Counsel for the carriers told the Board that Western received from the Bureau of Internal Revenue under date of May 1, 1951, an audit of the carrier's tax returns for 1947, 1948, and 1949. He also said the audit showed Western had a "tax deficiency liability" for 1947 several times larger than the Board proposed to allow in the tentative decision. As far as we can ascertain it appears that the statement of Counsel at the oral argument was predicated on Western's reporting as income for tax purposes the temporary mail pay received by the carrier pursuant to the Board's order of February 25, 1949 (Order Serial No. E-2506). As we indicated in the tentative decision, and as we point out below, the temporary mail pay received by Western under that order was substantially in excess of the fair and reasonable

In the case of Inland we find that the allowance for taxes to be included in the mail pay is \$66,154 based on a net taxable income of \$107,938 for the past period.

Conclusion

In view of the foregoing revisions of our tentative decision, we find that Western is entitled to receive total final mail pay of \$3,909,027. Since Western has received temporary mail pay of \$4,252,000 for operations during the period under review, we now find that the carrier has received an overpayment of \$342,973.

Recomputation of the proper tax allowance for Inland has also resulted in a change in the amount of final mail pay to be fixed for the past period operations of that carrier. Thus, we find that for the period April 1, 1947-December 31, 1948, Inland had a break-even need of \$858,000 to which must be added \$107,730 representing return on investment. Total final mail pay for this period, including \$66,154 as an allowance for taxes, is established at \$1,031,884. 3841 To this amount must be added \$6,000 mail pay due the carrier for the carriage of mail during the period March 28-31, 1947, inclusive, which is also part of the review period. Thus, total final mail pay for Inland for the entire past period under consideration is fixed at \$1,037,884. Having received \$1,099,000 in the form of temporary mail pay for the past period, Inland has been overpaid by \$61,116. Accordingly, IT IS ORDERED THAT:

1. Insofar as the opinion accompanying Order Serial No. E-4870, adopted November 24, 1950, is inconsistent with the findings made herein the opinion shall be, and it is, hereby modified in accordance with the said findings;

final rate of mail compensation to which the carrier was entitled for the past period. While it would have been desirable to have the additional information to which Counsel for Western referred, the carrier has not offered this information in evidence. Under the rules, a carrier may of course file a petition for reconsideration supported by an affidavit setting forth any newly discovered facts as regards its tax liability.

2. The third and fourth paragraphs of Order Serial No. E-4870, adopted November 24, 1950, be, and they are, hereby amended in their entirety to read as follows:

IT IS ORDERED, That the fair and reasonable final rate of compensation to be paid Western Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its routes within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada, for the period May 1, 1944-December 31, 1948, inclusive, is hereby fixed, determined, and published to be the amount of \$3,909,027.

IT IS FURTHER ORDERED, That the fair and reasonable final rate of compensation to be paid Inland Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its entire system for the period March 28, 1947-December 31, 1948, inclusive, is hereby fixed, determined, and published to be the amount of \$1,037,884;

3842 3. All exceptions not specifically mentioned in this opinion be, and they are, hereby overruled;

4. The final mail rates provided in Order Serial No. E-4870, adopted November 24, 1950, as amended herein, be, and they are, hereby made effective.

Nyrop, Chairman, Ryan, Lee, Adams, and Gurney, Members of the Board, concurred in the above opinion and order.

(SEAL)

/s/ M. C. MULLIGAN
M. C. MULLIGAN
Secretary

3844

BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2870 *et al*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

INLAND AIR LINES, INC.

Over its Entire System, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate transportation and over its routes between the United States and terminal points in Canada.

Petition to Reconsider.

TO THE CIVIL AERONAUTICS BOARD:

The Postmaster General, pursuant to Section 302.11 of the Board's Rules of Practice, hereby petitions the Board to reconsider the ruling for mail rate-making purposes which disregards as a proper offset against subsidy needs the net profit resulting from the sale of a route certificate, which ruling is set forth in the Board's Opinion and Order, E-5467, of June 26, 1951, in the above-entitled rate proceeding. The said ruling is challenged herein on the grounds that:

I

The mail rate section (406(b)) of the Civil Aeronautics Act does not permit the Board discretion to disregard the net revenues derived from the sale of a route certificate when determining the carrier's need for subsidy mail
3845 compensation.

II

The Civil Aeronautics Act, other similar regulatory acts, and all regulatory history specifically aim at the elimination of any certificate or franchise value when fixing rates. Yet the Board by this ruling not only gives the franchise a monetary value by allowing it to be the basis for a profit to the carrier, but also refuses to offset this profit against the carrier's subsidy need.

In support of the above two grounds for reconsideration of such ruling, the following is presented.

I

THE MAIL RATE SECTION (406(b)) OF THE CIVIL AERONAUTICS ACT DOES NOT PERMIT THE BOARD DISCRETION TO DISREGARD THE NET REVENUES DERIVED FROM THE SALE OF A ROUTE CERTIFICATE WHEN DETERMINING THE CARRIER'S NEED FOR SUBSIDY MAIL COMPENSATION.

The Board in its latest opinion of June 26, 1951, states: "While we are required by the Act to 'take into consideration' the 'need' of the carrier for mail compensation together with 'all other revenue', we do not understand the language of Section 406(b) as requiring us to reduce the carrier's mail pay 'need' with any part of such 'other revenue'. This is a matter within our discretion. That is, we may take in 'other revenue' in whole, in part, or not at all." (Page 5 of Opinion and Order E-5467.)

The Postmaster General contends that the mail rate section of the Act permits no such discretion when treating with the net profit on the sale of a route certificate.

Section 406(b) of the Act requires the Board in determining mail pay to consider:

"* * * The need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management to maintain and

continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.”

3846 If there is any discretion granted by the above statutory language, it is the discretionary power to grant or not to grant a subsidy over and above a service rate for the performance of actual mail service. *Chicago and Southern, Mail Rates*, (1941) 3 C.A.B. 161, 190. However, in the consideration of whether the development of air transportation requires a subsidy to a particular carrier in addition to compensation for services rendered, as directed by the same section, the Board has no discretion under such section but must take into account all other revenue of such carrier obtained from all sources. *T.W.A., Mail Rates*, (1943) 4 C.A.B. 139, 143. In this proceeding the Board has determined that a subsidy is needed over and above a service rate. The exact amount of subsidy is determinative on the basis of the carrier's other revenues. The carrier has been found by the Board to have obtained in other revenues \$447,000 as the net profit on the sale of a route certificate.

Since the carrier has received that money from such other sources, it has no “need” for which it may be paid again by additional compensation of \$447,000 as subsidy in the mail rate. *Pan American, Alaska, Mail Rates*, (1944) 6 C.A.B. 61, 67.

In this rate proceeding the Board has already determined that there can be no doubt that the transfer of the Route 68 certificate and equipment used in its operation involved air carrier property in every possible construction of the term. The Board also determined that the profits from the sale of the certificate and the equipment were realized by virtue of benefits accruing to the carrier from its certificate received from the government. As a result, the Board in its initial opinion hereon stated: “While this same certificate also entitled the carrier to subsidy mail pay to cover its need for

revenue under honest, economical, and efficient management, *it would be contrary to the public interest to use public funds to subsidize a need which had already been covered by profits accruing from the benefits under the certificate.*" (Page 17 of Opinion and accompanying Order E-4870, November 24, 1950, this docket. Italics supplied.)

Now, however, the Board by its latest opinion of June 26 (Order E-5467) has determined that the net profit can be broken into two parts for rate-making purposes; the profit on the equipment—the tangibles—is to be taken into account when fixing the carrier's need, but the profit from the sale of the certificate—the intangible element—is to be disregarded when determining the proper subsidy needed by the carrier. In this latest opinion the Board reaffirms its November 24, 1950 decision to the extent that the entire profit on both tangibles and intangibles was clearly a part of all other revenue of the carrier during the period under review. (Pages 4-5 of Opinion and Order E-5467.) Nevertheless, the Board now rules that it has the discretion to disregard the revenue obtained from the sale of the certificate as distinguished from the equipment and has decided not to offset this profit against the carrier's actual needs. (Page 9 of Opinion and Order E-5467.) If the profit on the route certificate, as so determined by the Board, is other revenue of the carrier, the Board has no discretion in the matter but must offset such profit against the carrier's need. The fact that part of the entire profit may be assignable to the route certificate only lends greater weight to the fact that the profit on such intangibles should be offset against any actual need for subsidy. If the Board recognizes that the profit obtained from tangible property of the carrier used in the carrier's operations under the certificate is other revenue, then surely the profit from the intangible—
 3848 the route certificate, which carries no property rights against the public—must with greater force be recognized as a source of other revenue to be deducted from the subsidy needs of the carrier.

This latter point will be developed more fully in Item II.

II

THE CIVIL AERONAUTICS ACT, OTHER SIMILAR REGULATORY ACTS, AND ALL REGULATORY HISTORY SPECIFICALLY AIM AT THE ELIMINATION OF ANY CERTIFICATE OR FRANCHISE VALUE WHEN FIXING RATES. YET THE BOARD BY THIS RULING NOT ONLY GIVES THE FRANCHISE A MONETARY VALUE BY ALLOWING IT TO BE THE BASIS FOR A PROFIT TO THE CARRIER, BUT ALSO REFUSES TO OFFSET THIS PROFIT AGAINST THE CARRIER'S SUBSIDY NEED.

The Board in its latest opinion of June 26 admits "we know of no controlling reason why the carrier's need should be duplicated by the net profit from the sale of the tangibles"—the operating equipment—, and accordingly the Board offsets this part of the profit against the carrier's need. (Page 8 of Opinion and Order E-5467.) If this operating equipment in which the carrier had a vested interest brings a profit on the sale thereof, which profit the Board includes as "other revenue" in determining the proper subsidy, then there is even greater reason to include as "other revenue" the profit on the sale of a route certificate in which the carrier has no vested interest.

The Civil Aeronautics Act specifically provides that "No certificate shall confer any proprietary, property, or exclusive right." (Section 401(j) of the Act.) The certificate is a matter of free public grant. The holder of the certificate holds it for the benefit of the public. Any value of the certificate belongs to the public. The public has made the sole contribution to the value placed on the certificate and has already paid for that value. The public should not now be forced to pay again for such value. The Board has recognized that such payment has already been made by 3849 the public when treating of the acquisition of the certificate by United by insisting that the value of the certificate be excluded from United's investment base. (See "Conditions to Approval", *United-Western, Acquisition*

Air Carrier Property, (1947) 8 C.A.B. 298, 318-319.) Thus, the public in that route sale case was not required to pay United again for the intangible value of the certificate. But now the board, in its opinion of June 26, by excluding such profit from Western's other revenues and thereby ruling that Western has a need for subsidy in an additional amount of \$447,000 in this rate proceeding, has in effect determined that the public must pay again, not to United, but to Western, the carrier which has already reaped the benefits accruing under the intangible—the certificate.

Other regulatory acts have similar provisions to the effect that certificates or franchises do not confer any proprietary or property rights. (See Part II of the Interstate Commerce Act, the Motor Carrier Act (49 U.S.C.A., Section 307(b)). See also, Federal Communications Act (47 U.S.C.A. 151, 301, et seq.) The courts have also recognized that such similar acts confer nothing in the nature of a vested interest or a property right as a result of the granting of a certificate. (See *A. B. & C. Motor Transport Co. v. United States*, (1946) 69 Fed. Sup. 166, 169; *F.C.C. v. Sanders Radio Station*, (1946) 309 U.S. 470, 475; *Ashbacker Radio Corp. v. F.C.C.*, (1945), 326 U.S. 327, 331.)

As early as 1923, the Supreme Court definitely ruled against the inclusion of franchise values in rate bases. *Ga. Ry. and P. Co. v. Commission*, (1923) 262 U.S. 625, 632.

Perhaps the best authority for the statement that regulatory history specifically aims at the elimination of any certificate or franchise value when fixing rates is the Board's own statement to that effect in its opinion approving 3850 this very sale of Route 68 by Western to United:

“* * * The regulatory policy to which this Board and other public utility regulatory bodies of the National and State Governments have adhered, and which recognizes reasonable market value with its ever present intangible elements as the basis for exchange transactions, but which refuses to allow such intangibles to be reflected in rates, cannot adversely affect the public users of the service. There

is no theory of logic or principle of economics that can include in a rate base an amount that has been excluded or that can collect from the public in increased rates a cost that has been excluded by the rate-making body. An economic theory which holds otherwise is at war with realities. The intangible elements of value in the purchase price, under such a policy as that to which this Board adheres no more enter the rate base than does the excess of market over book value of the carrier's capital stock. The effectiveness of this method of protecting the public through disallowances from both investment and operating expense in a rate proceeding would appear to be so well established in public regulatory experience as not to be subject to serious question." *United-Western, Acquisition Air Carrier Property*, (1947) 8 C.A.B. 298 at 322.

The Board, by the above statements, intended to leave no doubt when approving the sale that the public "cannot be adversely affected"; that "there is no theory" "that can collect from the public in increased rates"; that "the intangible elements of value" "no more enter the rate"; and that "the effectiveness of this method of protecting the public" is such "as not to be subject to serious question".

The Board in its opinion of June 26 states that the opinion in the route sale case "must form the keystone of our decision here" in this Western rate proceeding. (Page 6 of Opinion and Order E-5467.) How does the Board now propose to protect the public interest so emphatically proclaimed in that route sale case? By recognizing and placing a monetary value of \$447,000 on the route certificate; by finding that the selling carrier, Western, actually made that profit; by disregarding such profit as other revenue of Western, with the result that Western can now collect another \$447,000 in subsidy in the mail rate from the public—the very same unseen public the Board was so positive it was protecting in the route sale case.

The propriety of whether there should have been a profit on the sale of a certificate is, of course, a separate question not before the Board in this present rate proceeding. The fact remains, however, that the Board now determines that a \$447,000 net profit did actually occur; and thus, the Board

in this rate proceeding has no discretion under the rate-making section of the Act, but must offset such actual profit as "other revenue" against the actual needs of Western for a subsidy. To do otherwise would not only be contrary to the letter and spirit of the Act, but would only aggravate the situation and open wide the door to the barter and sale of certificates for subsidy for the private gain of such subsidized carriers to the detriment of the public.

A rate-making principle which on the one hand recognizes that a carrier has made an actual profit on the sale of a route certificate and on the other hand refuses to offset this profit against the carrier's need for subsidy clearly merits reconsideration and is grounds for appealable error.

CONCLUSION

Accordingly, the Postmaster General respectfully petitions the Board in this proceeding,

(a) to reconsider the ruling in its Opinion and Order of June 26, 1951 (E-5467) whereby the net profit on sale of a route certificate is being disregarded as other revenue when determining Western's subsidy need; and

3852 (b) to readopt the principle set forth in its Order E-4870 of November 24, 1950, which takes into account such profit when fixing Western's subsidy need.

ROY C. FRANK
(SIGNED) ROY C. FRANK
ROY C. FRANK
Solicitor
Post Office Department

FREDERICK E. BATRUS
(SIGNED) FREDERICK E. BATRUS
FREDERICK E. BATRUS
Assistant Solicitor
EUGENE J. BRAHM
(SIGNED) EUGENE J. BRAHM
EUGENE J. BRAHM
Chief, Air Mail Section
July 27, 1951

* * * * *

3857

BEFORE THE
CIVIL AERONAUTICS BOARD

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefore, and the services connected therewith, of

INLAND AIR LINES, INC.,

over its entire system, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

**Petition of Western Air Lines, Inc.,
For Rehearing, Reargument and Reconsideration.**

Pursuant to the authority of Section 302.11 of the Board's Economic Regulations, Western Air Lines, Inc. (hereinafter referred to as "Western"), respectfully petitions for a rehearing, reargument and reconsideration of the Board's Opinion and Order, Serial No. E-5467, adopted June 26, 1951, in the above-entitled proceeding.

I

SPECIFICATION OF NEW MATTER.

1. By Bureau of Internal Revenue audit report dated May 1, 1951, Western is liable for the payment of \$302,784.52 in Federal income taxes, applicable to the retroactive 3858 period at issue in the proceeding.

2. Petitioner, with due diligence, could not have known or discovered said new matter prior to the time of hearing in this case.

II

SPECIFICATION OF ERRORS.

1. The Board erred in adopting the so-called "tax return method" of computing the allowance for Federal income taxes.

2. The Board erred in considering as "other revenue" the profit from the sale of Route 68 and the profits from concessions operated by Western, in determining Western's mail pay requirements for the period.

3. The Board erred in finding that the policy it announced in the *United-Western, Acquisition Air Carrier Property* case can be fulfilled by permitting Western to retain only part of the profit from the sale of Route 68.

4. The Board, in treating with the Route 68 profit, erred in offsetting as deductions from the profit received from the sale of the intangibles certain losses and expenses incurred in connection with the sale of the tangible property.

5. The Board erred in adjusting Western's mail rate retroactively to May 1, 1944.

III

GROUNDS RELIED UPON IN SUPPORT OF THIS PETITION.

A. Introduction.

On December 30, 1948, the Board issued in this 3859 case a Statement of Tentative Findings and Conclusions and Order to Show Cause (Order, Serial No. E-2333). By that order, the Board proposed a final rate for the period May 1, 1944, through December 31, 1948, which provided for mail pay of \$975,000 in addition to that received under the tentative rate then in effect. By Orders, Serial Nos. E-2506 and E-2531, adopted February 25, 1949, and March 3, 1949, respectively, Western was awarded retroactive temporary mail pay of \$975,000.

On November 24, 1950, the Board issued its tentative decision and order fixing the final retroactive rate, holding that Western had received an overpayment of temporary mail

pay in the amount of \$671,474 for the period May 1, 1944, to December 31, 1948.

On June 26, 1951, the Board issued its final decision and order fixing the final retroactive rate of compensation for Western for the period May 1, 1944, through December 31, 1948, in which it found that Western had received an overpayment of temporary mail pay for the period under consideration in the amount of \$342,973.

We do not intend at this time to rehash the arguments made by Western in its prior briefs to the Board in this case. This petition is designed to supplement those two documents with new matters of law and fact which the Board should consider and has said it wants to consider. It is apparent from the Board's opinion and order disposing of Western's exceptions to the tentative decision that at least with respect to the allowance for Federal income taxes, the Board has not treated the subject with finality as far as

Western is concerned. A careful reading of footnote 3860 30 (page 26) to the Board's latest opinion in this case indicates that in the event the Board's findings with respect to the tax issue are contrary to the facts of this case, Western should file a petition for reconsideration supported by a proper affidavit setting forth the newly discovered evidence relating to Western's tax liability, which evidence is not a part of the present record. Accordingly, this petition is submitted in part for the purpose of calling to the Board's attention certain new matters relating to the issue of whether or not Western is entitled to a Federal income tax allowance in this case.

By this petition, Western will endeavor to convince the Board that on the basis of the Board's own findings, Western is rightfully entitled to additional mail pay over and above the Board's final retroactive rate in excess of \$500,000.

In our opinion the factual data which the Board must consider in passing upon the new issues raised by this petition are adequately and clearly set forth either in the present record or in the Appendices attached hereto and made a

part of this petition. If for any reason a serious question is raised which tends to minimize the probative value of the attached Appendices, it is respectfully requested that this proceeding be reopened for the purpose of permitting Western to introduce the information and data contained in the Appendices through a witness or witnesses, who will be prepared to stand cross-examination on the subject.

3861 *B. On the Basis of the Newly Adopted Tax Return Method Western is Entitled to a \$488,360 Allowance for Federal Income Taxes.*

In its final decision the Board has defined the tax return method to be applied in past period mail rate cases as meaning—

“... the technique of providing for a carrier's liability for income taxes on the basis of reliable evidence regarding the carrier's tax returns filed with the Bureau of Internal Revenue, *together with any adjustments made by the Bureau as of the most recent practicable date prior to the Board's order establishing final mail rates.*”*

The Bureau of Internal Revenue's audit of Western's tax returns for 1947 and 1948 was submitted to the carrier under letter from the Bureau dated May 1, 1951. It established a tax liability for Western in the retroactive period at issue, which fact was brought to the attention of the Board by counsel for the carriers during the course of oral argument on May 21, 1951. Evidence of that liability is proffered herewith for inclusion in the record of this case.¹

* Emphasis in quoted material added throughout unless otherwise noted.

¹ Pursuant to the Board's request made of Western through the Acting Chief of the Rates Division, Western submitted under date of June 6, 1951, a detailed exhibit analyzing Western's taxable income for the years 1944 through 1948 as reported on Western's Federal income tax returns and as adjusted by the Bureau of Internal Revenue. Copies of this exhibit were made available to all parties and all members of the Board. Western offered to stipulate all of the data contained in the exhibit and certain data outlined in the letter of transmittal of June 6. However, protracted negotiations with Public Counsel and the Postmaster General extending from June 6 until the issuance of the Board's final decision failed to culminate in an agreement with respect to stipulat-

3862 The foundation for the receipt of this newly discovered evidence was laid in the present record. On December 15, 1949, Mr. J. J. Taylor, Treasurer for Western, in testifying in this case before Examiner James M. Verner, made it amply clear that Public Counsel's Exhibit No. PC-47, on which Public Counsel and the Postmaster General have relied as the basis for establishing zero tax liability, did not in fact reflect Western's actual tax liability for the period under review (Tr. p. 206). Moreover, Mr. Taylor testified that it was impossible at that time to determine Western's actual tax liability (Tr. p. 208). He further pointed out that at that time the Bureau of Internal Revenue had audited Western's Federal income tax returns only through 1946, and, therefore, it was not then known what the Bureau of Internal Revenue would do with respect to the 1947 and 1948 tax returns (Tr. p. 211). Mr. Taylor also pointed out to the Examiner that until the Bureau of Internal Revenue had completed its audit of the 1947 and 1948 tax returns, and issued its report, it was impossible to conclude with finality whether the final mail compensation received for the period under consideration would
 3863 be considered as income in 1948 or 1949 or any other given year (Tr. pp. 203-213).

In response to the Board's suggestion contained in footnote 30, page 26 of its Opinion and Order disposing of Western's exceptions in this case, the following described exhibits and affidavits have been prepared and they are attached hereto and incorporated herein by reference and made a part of this petition for reconsideration:

ing this material because the other parties insisted that Western agree to include in the stipulation a provision that on the basis of the Board's tentative decision Western would not suffer any actual tax liability for the period in question. Obviously, Western could not have stipulated to such a provision because the provision is contrary to fact and to have so stipulated would have constituted a waiver of certain of Western's substantive rights in this proceeding. No doubt, the Board is familiar with the letter of June 6 and Western's offer to stipulate contained therein. That that factual material has not been received and made a part of the record is not the fault of the carrier.

Appendix No. 1—Western's Actual Tax Liability for the Years 1944 through 1948 as Established by the Bureau of Internal Revenue's Audit.

Appendix No. 2—Analysis of Taxable Income as Reported on Western's Federal Income Tax Returns and as Adjusted by Bureau of Internal Revenue for the Years 1944 through 1948.

Appendix No. 3—Western's Actual Tax Liability for the Years 1944 through 1948 on the basis of Adjustments Made by Bureau of Internal Revenue and Reflecting Final Retroactive Mail Pay Award Per Board Order, Serial No. E-5467, dated June 26, 1951.

Appendix No. 4—Analysis of Taxable Income Based on Western's Federal Income Tax Returns for the Years 1944 through 1948 as Adjusted by the Bureau of Internal Revenue and Reflecting Final Retroactive Mail Pay Award Made by Board Order, Serial No. E-5467, dated June 26, 1951.

Appendix No. 5—Affidavit of Mr. J. Judson Taylor, Treasurer of Western Air Lines.

Appendix No. 6—Affidavit of Mr. Eugene J. Patton, Manager of the Tax Department of the Los Angeles office of Peat, Marwick, Mitchell & Co., Certified Public Accountants.

Appendices 1 and 2 should be considered together. Appendix No. 1 establishes that on the basis of Western's tax returns for the years 1944 through 1948, as audited by the Bureau of Internal Revenue, the result of which audit is reflected in its reports dated February 17, 1948, and May 1, 1951, *Western has an actual tax liability for the rate review period in the amount of \$302,784.52.* Additionally, that on the tax deficiency of \$302,784.52 the Bureau of Internal Revenue will assess Western interest estimated at \$25,000. Appendix No. 2 is an analysis of the taxable income as reported on Western's income tax returns and as adjusted by the Bureau of Internal Revenue for the years 1944 through 1948. All of the data and information in Appendix No. 2 are taken from either the tax returns or the Bureau of Internal Revenue's audit reports.

In connection with Appendices 1 and 2, it must be pointed out that the tax liability of \$302,784.52 (which would require a mail pay allowance of \$488,360, for reasons hereinafter discussed) is based on a determination that the \$975,461.20 retroactive temporary mail pay received in 1949 pursuant to Orders, Serial Nos. E-2506 and E-2531, adopted February 25, 1949, and March 3, 1949, respectively, should have been reported as income in 1948. Western reported that temporary mail pay as income in 1949. However, the Bureau of Internal Revenue ruled that inasmuch as the retroactive mail pay received in 1949 was for services rendered in 1948, under I. T. 3961 (CB 1949—2, p. 35) such income accrued for Federal income tax purposes in 1948. This accounts for the adjustment in item 8 of Appendix No. 2

3865 Another significant adjustment made by the Bureau of Internal Revenue pertains to Convair training costs incurred in 1948 and which Western deducted for income tax purposes in that year. It was ruled that this expense must be amortized over a five (5) year period in conformity with the Board's treatment of those costs for mail rate purposes. This explains the adjustment in item 9 of Appendix No. 2.

Appendix No. 1 reveals Western's tax liability at the applicable 38% rate on the basis of the "tax return method." Allowance of that item (\$302,784.52) would increase Western's net taxable income to a point that an allowance of \$488,360 would be required, computed as follows:

$$\begin{aligned} x &= \text{Income Tax Allowance} \\ x &= 38\% (796,838.10 + x) \\ x &= \$302,784.52 + .38x \\ .62x &= \$302,784.52 \\ x &= \$488,360^2 \end{aligned}$$

²Proof of correctness of income tax allowance:

| | |
|---|-----------------------|
| Net Taxable Income 1944-1948 (Appendix No. 2) | \$ 796,838.10 |
| Add: Additional mail pay Western entitled to receive as allowance for tax liability of \$302,784.52 | 488,360.00 |
| Adjusted Net Taxable Income | <u>\$1,285,198.10</u> |
| Federal Income Tax on \$1,285,198.10 at 38% | <u>\$ 488,360.00</u> |

On the basis of the Board's final decision in this proceeding Western's retroactive mail pay for the period is reduced from \$975,461.20 to \$632,488.20. Notwithstanding that reduction, Western will still have actual tax liability. *However, on the basis of the Board's "tax return method" as defined in its final opinion, Western is entitled to an income tax allowance of \$488,360 in order to pay the existing tax liability of \$302,784.52, plus an additional allowance for interest due on the tax deficiency.* On the other hand, if the Board decides to abandon or modify its announced "tax return method" in order to reflect the decrease in retroactive mail pay and make its allowance on that basis, Western will still be entitled to an allowance for Federal income taxes of \$278,175.39, plus interest, in order to underwrite an actual tax liability of \$172,468.76.

Inasmuch as Western's tax returns for 1944, 1945 and 1946 have been signed off by the Bureau of Internal Revenue and Western has accepted the Bureau's audit of the 1947 and 1948 returns, Western will probably pay the tax liability of \$302,784.52, plus \$25,000 interest thereon, within the next thirty (30) days. At this late stage it does not appear likely that it will be possible to effect any further amendment to the 1947 and 1948 returns and audit. Assuming that that situation prevails, Western's only other recourse, in the event the Board grants a tax allowance commensurate to adjusted actual tax liability, *i.e.*, an allowance of \$278,175.39, would be to file for a tax refund, the amount of which, of course, would depend on the amount of the Board's final allowance for taxes.³

3867 Appendix No. 4 has been prepared in order to establish Western's actual taxable income for the period under the Board's final decision in this proceeding, *i.e.*, reducing retroactive mail pay from \$975,461.20 to \$632,-

³ Assuming tax liability on taxable income as per Board's final decision (See Appendix No. 4) the proper tax allowance is \$278,175.39. Therefore, Western would have been overpaid \$64,797.61 instead of \$342,973. On that basis Western would be entitled to a tax refund of \$24,637.05, which would result in a total tax of \$278,175.39, for which allowance is herein proposed.

488.20. With that adjustment the actual tax liability (not to be confused with income tax allowance as part of the return element) as revealed by Appendix No. 3 is \$172,468.76. On the basis of \$172,468.76 tax liability, Western is entitled to an income tax allowance of \$278,175.39, computed as follows:

$$\begin{aligned} x &= \text{Income Tax Allowance} \\ x &= 38\% (\$453,865.10 + x) \\ x &= \$172,468.76 + .38x \\ .62x &= \$172,468.76 \\ x &= \$278,175.39^4 \end{aligned}$$

⁴ Proof of correctness of income tax allowance:

| | |
|---|--------------|
| Net Taxable Income 1944 through 1948 (See Appendix No. 2) | \$796,838.10 |
| Deduct mail pay to be refunded per CAB Order, Serial No. E-5467, adopted June 26, 1951 | 342,973.00 |
| | <hr/> |
| Add additional mail pay to which Western is entitled to cover allowance for actual Federal income tax liability | \$453,865.10 |
| | <hr/> |
| Adjusted Net Taxable Income | \$278,175.39 |
| Federal Income Tax on \$732,040.49 at 38% | \$732,040.49 |
| | <hr/> |
| | \$278,175.39 |

Appendix No. 5 is the affidavit of Mr. J. Judson Taylor, Treasurer of Western, and is considered to be self-explanatory.

Appendix No. 6 is the affidavit of Mr. Eugene J. Patton, Manager of the Tax Department of the Los Angeles office of the accounting firm of Peat, Marwick, Mitchell & Co., Certified Public Accountants, and it also is considered to be self-explanatory.

3868 Under the Board's theory as to the function of the tax allowance, Western is entitled to retain the return on investment awarded *free of taxes*. This principle is stated at page 19 of the Board's final decision:

"A third amount is also provided to cover Federal income taxes on the theory that if the carrier must pay taxes on the profit included in the mail rate, it will not, in fact receive the fair and reasonable rate to which it is entitled."

This is also in line with what the Board said in its amended statement in the *Pan American Transatlantic Rate*

case, (Order, Serial No. E-4561, adopted August 25, 1950): "The tax allowance is basically included in a mail rate because for mail rate purposes income taxes have been treated as costs, and the rate is intended to provide a profit margin above all recognized costs."

Applying such principle to Western's case, not only is the carrier entitled to an allowance of at least \$172,468.76 but, inasmuch as any allowance awarded is itself subject to income tax, the carrier is also entitled to an additional allowance in the amount of at least \$105,706.63, or a total allowance of at least \$278,175.39.

Moreover, because under the Board's theory Western should be left after taxes with the profit element included in the mail rate, it follows that in the circumstances of this case allowance must also be made for the estimated interest on the tax deficiency amounting to approximately \$25,000. The reason for that assessment of interest is to be found in the workings of the carry-forward, carry back provisions of the tax law and not in any default on the part of the carrier. On the basis of an estimated interest expense of \$25,000⁵ the allowance therefor comes to \$40,322, computed as follows:

$$\begin{aligned} x &= \text{Allowance} \\ x &= \$25,000 + .38x \\ .62x &= \$40,322 \\ x &= \$25,000 \end{aligned}$$

In summation, it is apparent from the foregoing discussion and a careful analysis of Appendices 1 through 6 that on the basis of the Board's newly announced tax return method, Western is entitled in this proceeding to an income tax allowance of at least \$278,175.39, plus an additional allowance for interest.

⁵ The \$25,000 interest on the tax deficiency is an estimated figure (See Appendices 1, 3 and 5). However, if the Board wants to withhold making that allowance until it is apprised of the exact amount, it is suggested that this matter be kept in abeyance pending final determination. It is opined that the \$25,000 estimate approximates actual liability and, therefore, the car-carrier is willing to accept that figure as final.

C. The Method Adopted by the Board for Determining the Federal Income Tax Allowance is Unworkable and Will Delay the Disposition of Pending Rate Cases.

Adoption of the "tax return method" for determining the income tax allowance in retroactive mail rate cases appears to be another step toward making the Board's work more difficult and complex without any corresponding benefit to the public interest. Not too many years ago the Board was able to dispose of mail rate proceedings without any unreasonable delays. Now it takes the Board several years 3870 to process a rate petition during which time the carrier's financial status is indeterminable. The situation is becoming increasingly worse. For example, in the fiscal year 1950, the Board issued 8 final mail rate decisions for domestic carriers, 3 relating to trunklines and 5 to feed-erlines. With 12 new final rate proceedings opened by petition or by Board order and only 8 cases closed, the backlog of final mail rate proceedings increased from 24 at the beginning to 28 at the close of that fiscal year.⁶ With respect to international and overseas carriers, there were 21 final mail rate proceedings pending at the beginning of the year and although a number of show cause orders were issued by the Board during that period, the close of the fiscal year 1950 still found 22 final mail rate proceedings pending.⁶ These facts are pointed to not in criticism of the Board, for we know that the Board is deeply concerned with this situation, but because after three years of actual litigation in this proceeding and the lapse of more than seven years since the filing of the initial petition in this case, it is our considered opinion that probably one of the principal reasons for the unreasonable delay experienced in this and other rate proceedings is the growing tendency on the Board's part, and particularly on the part of its staff, to pursue a "delusive exactness" which, in our opinion, is impossible of attainment by the Board or any other administrative agency or

⁶ Annual Report of Civil Aeronautics Board, 1950, pp. 12-13.

commission called upon to perform the important, but complicated, function of rate fixing.

3871 Considering all that has been written and said in this proceeding with respect to the issue of appropriate Federal income tax allowance, it is our opinion that probably the "windfall" argument belabored by the proponents of the so-called "actual tax liability" method forms the keystone of the Board's decision to adopt the tax return method. In the preceding section of this petition we have demonstrated that by applying the tax return method, or the actual tax liability method, Western is entitled to an income tax allowance in this case of either \$278,165.39 or \$488,360, exclusive of any allowance for interest. So if there is any merit to the so-called "windfall" argument in this case, it involves not \$600,000, as contended by the Postmaster General and Public Counsel, but between \$100,000 and \$300,000. Recognizing that in this proceeding involving a fifty-six (56) month period the Board has had to review reported non-mail revenues approximating \$33,450,000, and expenses in excess of \$38,400,000, we submit that if in fixing the rate the Board comes within several hundred thousand dollars of pegging the so-called *exact* rate, it has done not only an outstanding and commendable job, but one which will be duplicated only in very rare instances by the Board or any agency. Time and time again the Board has said that rate fixing is not subject to mathematical precision. On the contrary, rate fixing involves the exercise of sound judgment. In the language of the Supreme Court of the United States, "The process of rate making is essentially empiric." *Board of Trade v. U. S.*, 314 U. S. 534, 546, 86 L. ed. 432, 443 (1942). The result, at best, is an informed estimate.

3872 That the constructive method of computing the income tax allowance has resulted in any "windfall" to the carriers involved in any of the 45 to 50 mail rate cases decided by the Board during the past ten years in which the method was employed *has not been demonstrated in this case*. It could not be, for as the Board said at page 18 in its final decision in this case:

"This appears to be the first case to have come before us in which it has been shown that the customary constructive tax basis would result in awarding the carrier an amount for income taxes which has not been, and will apparently not be, disbursed, and which must, therefore, be considered a windfall to the carrier."

If no "windfalls" have occurred in previous cases, then why does it become necessary to adopt a new method in this case about which method the Board already has said that "in practice . . . basic difficulties might well be encountered in the administration of such a policy," and "that the determination of actual tax liability is not considered feasible"? In effectuating a change in policy on as important an issue as this, the Board should require that the proponents of the actual liability method come forward with clear and convincing evidence showing that the practice they propose to have changed has resulted in the dissipation of public funds. No such evidence has been produced. Both the Postmaster General and Public Counsel had the opportunity to introduce such evidence but chose not to for the obvious reason that such proof is totally lacking. Public Counsel conceded that fact in oral argument before the Board prior to the issuance of the final decision in this case

(Tr. p. 87). Therefore, the idea boils down to what 3873 the Postmaster General has repeatedly said on brief and in argument to the Board in this case, that is, that the Board should *not* concern itself with long-term policy but should consider just what prevails in Western's case, and if there is any "windfall," that it should be eliminated, notwithstanding the fact that this would require an important change in policy which could seriously hamper the Board's rate fixing ability. That position, however, does violence to one of the Board's most important cardinal rules. The Board has repeatedly stated in mail rate proceedings that adoption of a "keyhole view" in rate making is repugnant to the provisions of the Act and what Congress intended.

We are surprised that the Board, busily concerned with problems of reorganization, and doing everything possible to speed the handling and furtherance of mail rate proceedings, should permit itself to be convinced by such arguments to the extent of adopting a new policy which poses serious and complex administrative problems that cannot be brushed aside in such a cavalier fashion as suggested by the proponents of the actual tax liability method.

Without trying to minimize the importance to Western of the tax allowance dollars involved in connection with this case, we maintain that the Board must bear in mind that Western is concerned with the application of the tax return method not only in this proceeding, but also as it applies to future mail rate proceedings. Therefore, what the Board should really focus on in this case is the question of whether

there is a *need* for a change in policy. It should be
 3874 significant to the Board that the Air Transport Association of America intervened in this proceeding as *amicus curiae* and took a very definite position *against* both the "hybrid" method adopted in the tentative decision and the "actual liability method" proposed by the Postmaster General and Public Counsel. The ATA is submitting a brief in this case and in presenting oral argument before the Board had no "ax to grind" for Western. It appeared at the request of its entire membership, who undoubtedly, after having analyzed the proposed new tax policy, concluded that such policy was not feasible, that it was impossible to administer, that it gave rise to many inequities in fixing rates, and last but not least, that it would saddle the Board with the responsibility of determining actual tax liability, a subject which all readily admit is fraught with complexities.

We do not intend to repeat the arguments made against the "hybrid" method and the actual tax liability method, for we believe that those arguments have been adequately discussed by Western and the ATA in their briefs to the Board and in oral argument. Suffice to say that in our

considered opinion the change in policy is not justified on the basis of experience. Need for the change in policy has not been established. Therefore, in reconsidering this matter it is urged that the Board give serious consideration to supplying the answers to the problems and questions hereinafter discussed which we think are inherent in the application of the tax return method.

For example, let's assume carrier A had its retroactive rate finalized on December 31, 1950, that period reviewed involves four years and that as of December 31, 1950, 3875 the Bureau of Internal Revenue has not completed its audit nor has it issued its audit report. Under the Board's tax return method, the tax allowance is to be based on the tax returns filed by the carrier. However, assume further that on June 1, 1951, the Bureau of Internal Revenue issues its audit report and assesses a tax deficiency for the period ending December 31, 1950. There is no question but that under the Board's theory the carrier is entitled to be compensated for that tax liability as part of the element of return. However, how will recovery be effected? Will the carrier be permitted to file a petition for reconsideration on the grounds of newly discovered evidence and if so, will the Board reopen the mail rate proceeding involving the rate finalized as of December 31, 1950? If so, will other parties such as Public Counsel or the Postmaster General then be permitted to raise any other issues with respect to that proceeding? Or, if the suggested procedure is not acceptable, can the carrier then file a rate petition immediately seeking recovery of the amount of tax deficiency? If the carrier is on a temporary rate at that time, *i.e.*, June 1, 1951, presumably the tax deficiency might be treated as an additional cost of doing business within that period. However, if the carrier is on a final rate, will the filing of a rate petition, limited to seeking recovery for tax deficiency, open the carrier's entire rate? On the basis of the Board's decision in this case, the entire rate would be

opened because the Board has refused to recognize that a rate petition may be limited in nature. If the filing of a limited rate petition opens the entire rate, how will that procedure help solve the Board's problem of trying to keep carriers on a permanent rate? These are but a few of the innumerable questions which must be answered. We do not intend to be "alarmists" in the matter, but under the present tax structure many carriers, we venture to say, will have Federal income tax liability as great as, or in excess of, the amount of mail compensation they may be receiving from the government. Therefore, the possible discrepancies will be substantial, not "minor" as suggested by Public Counsel in recent oral argument.

Furthermore, let's assume again that carrier A's rate for a retroactive period is finalized December 31, 1950, at which time the Bureau of Internal Revenue's audit has not been completed. Under the "tax return method," will the Board limit its determination of tax liability to what the returns disclose, or will it also consider such liability *as may arise* by adjustments after audit? If so, will that determination be final regardless of what the Bureau of Internal Revenue's audit discloses at some future date? If that procedure is to be followed, and the Board's language seems to suggest that practice, then is it not a fact that the Board, in effect, will *estimate* the tax liability?

Additionally, let's assume that the particular rate review period and the taxable period do not coincide, which will probably be the rule in most situations. On what basis would the Board apportion taxes as between the period under review and the period not under rate review? Similarly, how would the Board apportion mail pay as between those two tax periods? Public Counsel in oral argument (Tr. pp. 82-84) indicated that the Board's staff does that every day. However, there is no evidence in this record as to how that could be accomplished

or that there would be any necessity for making such apportionment.⁷

Let's assume a carrier operates more than one division. How would the Board determine the actual tax liability for each division? The method suggested by Public Counsel in oral argument certainly is no answer to the problem, particularly if the carrier files consolidated tax returns, as is the practice with a number of carriers.

How about the case of carrier B that is also engaged in non-transport activities? How would the actual tax liability be determined as between air carrier activities under review and non-transport activities? Would it be done by simple, straight line allocation as suggested by Public Counsel? If so, what happens when the loss carry-over and loss carry-back provisions of the tax law apply to such a situation?

The foregoing are but a few of the many, many questions which come to mind and are bound to arise in connection with the administration of the tax return method.

3878 In our considered opinion, it would be a mistake for the Board to brush aside these questions by merely stating that they will be answered when the situations arise, because if the change in policy is to be made, and this is a policy decision with respect to the tax allowance issue, then the Board should consider the possible disadvantages and problems resulting as well as the alleged benefits, particularly since there has been no showing made in this proceeding that application of the constructive tax basis is contrary to the public interest.

It has been demonstrated that the tax return method adopted by the Board in its final decision is no easy thing to administer but further complicates the Board's work. This was considered the easy or simple case. But applica-

⁷ Again it must be pointed out that only Western introduced evidence in this case with respect to the imponderables in the use of an actual tax liability method. In fact, Public Counsel has always taken the position that the income tax issue raised only a question of law. See Tr. p. 204 wherein Public Counsel stated:

"... I think that we are dealing now [talking about federal income tax issue] solely with the question of law rather than with the question of fact...."

tion of the adopted method here has not proved simple. Accordingly, we urge that in rate proceedings, the Board adopt such policy as will result in like treatment for all carriers, is consistent with the Act, and is easily administrable, otherwise the public interest will not be served.

3879 *D. The Board Erred in Considering as "Other Revenue" the Profit from the Sale of Route 68 and the Profits from Concessions Operated by Western in Determining Western's Mail Pay Requirements for the Period.*

The Civil Aeronautics Act empowers the Board to fix "... fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith..." Section 406(a). The Board is required to consider in determining the rate to be paid a particular carrier several important factors, including the cost for carrying the mail and the carrier's need for additional compensation which "together with all other revenue" of that carrier will be sufficient "to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." Section 406(b).

While the legislative history of the Civil Aeronautics Act affords no conclusive explanation of what was meant by Congress in Section 406 or any part of that section, at the threshold of every determination of so-called "subsidy" mail pay, the Board is confronted with a problem of statutory construction which the Board has described as at times "most difficult."⁸ In simple language, the question

⁸ "The meaning of 'all other revenue of the air carrier' which the Board is required to consider in fixing fair and reasonable mail rates under Section 406(b) is one of the most difficult phrases in the entire Act to interpret." *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C.A.B. 267, 289 (1947).

3880 is whether the phrase "all other revenue of the air carrier" is all-embracing or whether a restrictive meaning was intended by Congress. If the latter was intended, the Board, of course, is bound to observe that meaning.

In its brief in support of exceptions to the Board's tentative decision in this case, Western indicated the background of the language which Congress enacted into law as Section 406 of the Civil Aeronautics Act and illustrated that similar language in other statutes which was equally broad or broader in literal meaning had been interpreted judicially to have a less-inclusive content. Thus, under Section 6(e) of the Air Mail Act of 1934, the Interstate Commerce Commission was enjoined to consider, in fixing and determining the fair and reasonable rates of compensation for the transportation of mail by air, the carrier's "revenue and profits from all sources," among other things. Yet, when confronted with the contention that that provision was intended to mean strictly what it says, *i.e.*, revenue and profits from every conceivable source, the Commission rejected that proposition as not within the contemplation of the Air Mail Act. *Air Mail Compensation*, 206 I.C.C. 675 (1935).

Western does not contend necessarily that the Board is bound to exclude from "all other revenue" those items which the Interstate Commerce Commission has excluded as not being within the scope of "revenue and profits from all sources." Western does contend however, that the reasoning by which the Interstate Commerce Commission reached various decisions is proper and is the rationale which Congress intended the Board to employ in its mail rate deliberations.⁹

True, there are significant differences which can be described between the Civil Aeronautics Act and the Railway Mail Pay Act of 1916 and the Air Mail Act of 1934. The Board, however, failed to state that, even though the Air

⁹ "Rates for the carriage of mail would be fixed . . . in the same manner as the Commission now fixes the air mail rates for all domestic air-mail carriers." House Report No. 911, 75th Congr., 1st Sess., p. 18.

Mail Act was preoccupied with mail service and a route concept, a subsidy was provided for under airmail contracts. *Chicago and Southern Air Lines, Inc.—Mail Rates for Route Nos. 8 and 53*, 3 C.A.B. 161, 189 (1941). A strict interpretation of the phrase "revenue and profits from all sources" obviously would have permitted offsetting all such revenue against the mail pay need of a route. Yet, the Interstate Commerce Commission ruled that Congress did not intend an all-inclusive meaning to attach to the language of the statute. Similarly, we maintain that Congress did not intend "all other revenue" to embrace every conceivable form of income realized by the holder of a certificate of public convenience and necessity authorizing the transportation of mail by aircraft.

Once that proposition is admitted, and it has been admitted by the Board,¹⁰ the interpretation of the 3882 statute becomes a matter of pricking out a line between what is and what is not "other revenue." To the extent the Board is purporting to rule in this case, or in effect is ruling, that it has the power to consider income of the carrier from all sources, on the face of its decision the Board has erred. If that is not the import of the final decision in this case, although there is reason to believe that it is,¹¹ Western contends that the Board has con-

¹⁰ In determining Pan American's Transatlantic Mail Rates, the Board declared that the statutory language "could hardly have been intended to include revenues from every possible source unless the Act had intended that air carriers should not be permitted, at least so long as they might receive subsidy mail pay, to engage or invest in non-air-carrier activities. Yet there is no indication in the Act that such was its intent. Clearly, in determining need we could not consider net losses sustained by a carrier in non-air-carrier activities. To do so would result in Government subsidization of such activities through mail payments without any statutory authority therefor. Yet if we were to consider the profits from such activities to reduce need, we would place the carrier in the position of standing all losses from such activities but reaping no benefits from the profits so long as it remained on a subsidy basis." *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C.A.B. 267, 290 (1947).

¹¹ In the tentative decision in this case, the Board declared that "the mandate of the Act for underwriting the operations of need carriers includes the corollary consideration that all revenues generated by the air carrier be used first to reduce the contribution of the Government,

3883 sidered certain items of income realized by Western as "other revenue" which were not intended by Congress to be treated as "other revenue" within the meaning of Section 406(b).

Without reiterating the whole of Western's argument concerning this phase of the matter (the argument appears at pp. 11 thru 17 and pp. 30-32 of Western's brief of January 19, 1951), Western's position is that neither the profit from the sale of Route 68 nor the profits from the operation of restaurants, concessions, and slot machines can be so related to any air-carrier activity engaged in by Western as to permit their consideration as "other revenue of the air carrier." Is the Board willing to underwrite losses which occur in transactions of the type involved? If it would have no statutory authority to do that, it ought not to consider profits from those sources as "other revenue," otherwise the carrier would be obliged to stand the losses without benefit of the profits. *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C.A.B. 267 (1947).¹² Western does not concede and is not ready to concede, as the Board puts it, that profits from the operation of restaurants may be included as "other revenue." We chose to emphasize the income from slot machines, because that type of operation seemed so utterly unrelated to any air carrier activity
3884 engaged in by Western as to dictate clearly the ex-

unless compelling reasons dictate otherwise." Order Serial No. E-4870, November 24, 1950, p. 14.

In the final decision in this case, the Board declared, "... this profit [from the sale of Route 68] was clearly part of 'all other revenue' of Western during the period under review. The language of Section 406(b) of the Act can hardly be read otherwise . . . Western's net profit from the operation of restaurants, concessions, and slot machines is undoubtedly part of the carrier's 'all other revenue,' and we are aware of no consideration which advises against charging this revenue to the carrier's need for mail compensation." Order, Serial No. E-5467, June 26, 1951, pp. 4, 5, 11.

¹² In contrast to its reasoning in the cited case, the Board saw fit to remark in the tentative decision in this case, "The question as to whether the loss would be underwritten with mail pay is not controlling in determining whether the revenue should be considered as reducing mail pay." Order, Serial No. E-4870, November 24, 1950, p. 13n. Compare *Alaska Airlines, Inc., Mail Rates*, 9 C.A.B. 759 (1948).

clusion of such income from "other revenue" for mail pay purposes. In Western's opinion, the operation of slot machines represents the "lowest common denominator" of the type of activity which is not related to air-carrier operations. The hyperbole adopted by the Board in relating the operation of slot machines to Western's air-carrier activities at Las Vegas demonstrates the extent to which the Board has gone in this case in invoking the "other revenue" provision of Section 406(b) to decrease Western's mail pay need for the period in question.

With reference particularly to the sale of Route 68, the Board is confronted with a transaction involving the sale of capital assets resulting in a gain to Western. It appears significant to us that were the Board in this case fixing a retroactive *service* rate it could not consider the profit from that sale in determining the cost of carrying the mail. Only when the so-called "subsidy" factors of Section 406(b) are involved can the Board consider the "other revenue" of the carrier. Federal subsidy is not new, and the government's intent as to one type of subsidy ought to bear a relationship to its intent as to other subsidies, generally and in particular. Under the Air Mail Act of 1934, the Interstate Commerce Commission has excluded many forms of "revenue" in fixing mail rates, on the ground that Congress did not contemplate their inclusion. With respect to the operating-differential subsidy to the Merchant Marine, capital gains and capital losses are expressly to be disregarded. 46 U.S.C.A. §1176. Under the Civil Aeronautics Act, there is nothing to indicate that Congress intended capital gains and capital losses to be considered by the Board in the determination of a carrier's need.

While "revenue" often is utilized as a generic term, it is susceptible of a narrower meaning. Congress could have meant in this instance "revenue" derived solely from the operation of aircraft under certificates of public convenience and necessity. That that was the congressional intent com-

ports with the Interstate Commerce Commission's interpretation of what Congress had in mind in the Air Mail Act. It is the only reasonable interpretation of a statute which relates the need of a carrier to the maintenance and continued development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

E. The Policy Pronounced in the Acquisition Case Applies to the Entire Profit Realized from the Route 68 Sale.

The Board is absolutely right in concluding in its final decision that the views of the majority of the Board in the *United-Western, Acquisition Air Carrier Property* case, 8 C.A.B. 298 (1947), must form the "keystone" of its decision in this proceeding. The Board's decision in the *Acquisition* case states very clearly the policy which must control as to whether the profit from the sale of Route 68 shall be applied to reduce Western's need for mail pay for the period under review. The considerations spelled out in that case bottom the policy arguments of Western and the ATA in this proceeding. It is gratifying, to say the least, to see that the

Board has now recognized in its final decision in this 3886 case the importance of the considerations which must control the final disposition of the profit from the sale of Route 68 and has taken the opportunity in its final opinion to reaffirm in principle the declaration of policy made by the Board in the *Acquisition* case, by declaring that—

"In order to avoid the danger of confining the present air pattern to a rigid mold, and to continue to encourage voluntary action by the carriers, we believe that the incentive of profit which may be derived from the sale of a route so clearly approved in the *Acquisition* case should be preserved here."

However, if the views of the majority of the Board in the *Acquisition* case form the "keystone" of the Board's de-

cision in this proceeding, then it follows that Western should be entitled to retain the entire profit realized from the Route 68 sale transaction. At no time and at no place in the Board's opinion in the *Acquisition* case did it state, indicate, suggest or imply that the allowance of only a "part" of the commercial profit to be realized from the then proposed transaction would be sufficient incentive to bring about the improvement of the air pattern through voluntary action by the carriers. In the *Acquisition* case the Board was only thinking in terms of the profit on the entire transaction. For the Board to now conclude that it accepts and does justice to the views of the majority in the *Acquisition* case if it permits Western to retain a part of the profit from the sale transaction, is, at best, an administrative compromise. The record in the *Acquisition* case makes it amply clear that the sale of the route was condi-

tional on the sale of the aircraft and other tangible
3887 property (Tr. p. 49, Docket No. 2839). Additionally,

United would not have been able to operate Route 68 at the time of the sale unless it acquired the aircraft and facilities that Western utilized in providing service over Route 68.

The Board assumes that if Western had sold the operating property and the equipment involved in the transfer of Route 68 without reference to the certificate and other intangibles, that there would have been ample authority for holding that the profit from the sale of the tangible property should be applied to reduce the carrier's need to be met by mail pay. But Western would never have sold the tangible property separately. The indisputable facts of record in the *Acquisition* case are that but for the sale of Route 68 Western would not and could not have sold the aircraft and equipment in question for the obvious reason that the equipment and facilities would have been required in connection with the continued operation of Route 68. In fact, if Western had disposed of any of its aircraft, it would have been most difficult, if not impossible, for Western to have

provided adequate service over Route 68 and at the same time inaugurate service north of San Francisco to Portland and Seattle. Any assumption on the part of the Board in this case that Western could have sold four aircraft and other equipment "without reference to the certificate and other intangibles" does violence to the realities and practical business aspects of the situation. No matter how the Board may cut the pie in endeavoring to effect a compromise in this proceeding of the Board's policy pronouncement in the *Acquisition* case, the irrefutable fact 3888 remains that the sale of the aircraft and equipment was part and parcel of the transaction involving the sale of Route 68.

Accordingly, it appears to us that the Board has gone only part way in making the views of the majority in the *Acquisition* case the "keystone" of its decision in this proceeding. The Board is on sound ground as far as it has gone. But, to accomplish what was intended by the majority of the Board in the *Acquisition* case, the Board must in this proceeding permit Western to retain not only the profit from the sale of the intangibles but also the profit from the sale of the tangible property transferred in connection with the sale of Route 68. Therefore, it is respectfully urged that the Board reconsider this matter in light of the foregoing discussion and take the action required to make its decision in this case entirely consistent with the decision of the Board in the *Acquisition* case.

F. The Net Profit Realized from the Sale of the Tangible Property is \$529,000 and not \$652,000.

Assuming that the Board's decision permitting Western to retain only the profit on the sale of intangible property is within the Board's sound discretion and that it represents the exercise of sound judgment, Western contends that the Board has erred in not considering as proper offsets against the profit from the sale of the tangible property two items amounting to \$136,389. In the final decision in this case, the Board apparently concluded that (1) miscellaneous

charges relating to the sale amounting to \$32,389 and (2) loss on the retirement of DC-4 non-rotatable spare parts amounting to \$104,000 are chargeable as offsets against the profit from the sale of the intangible property instead of against the profit on the sale of tangible property, as contended by Western.

1. Miscellaneous Charges Relating to Route 68 Sale Amounting to \$32,389.

The miscellaneous charges relating to the *entire* sale transaction are as follows:

| | |
|--------------------------------------|------------------------------|
| Moving and storage of material, etc. | \$ 3,898 |
| Legal Fees and Expenses | 18,212 |
| Miscellaneous Expenses | 9,215 |
| Printing DC-6 maintenance manuals | 1,064 ¹³ |
| Total | <hr/> \$32,389 ¹⁴ |

¹³ This item should probably be eliminated. It is interesting to note that with the exception of this one item the Postmaster General has taken the position in this case that the remainder of the miscellaneous charges, involving the cost of moving, storage, legal fees, etc., amounting to \$31,325 should be allowed.

¹⁴ Exhibit Nos. W-53 and PC-17. Neither the amounts nor the nature of the expenses are in dispute because, as indicated by Public Counsel in PC-17, the information was obtained by an "audit of the books of the carrier by personnel of the CAB."

By way of explanation, the expense for the moving and storage of material was incurred in connection with the tangible property that was transferred. Therefore, about this item there can be no question. As to the legal fees and miscellaneous expenses, they were incurred in connection with the *entire* transaction and, therefore, there should be some equitable division of those costs. For example, part of the legal expenses and fees were incurred in obtaining abstracts covering the ownership of the tangible property transferred, preparing Bills of Sale, mortgage re-leases, etc. (Exhibit No. W-53). Therefore, all in all, with the exception of the item of printing DC-6 maintenance manuals, the remainder of the expenses amounting

to \$31,325 were incurred in connection with the entire sale and the consummation of the sale involving both the tangible and intangible property. Such being the case, there should be no question about offsetting at least a part of those expenses against the profit from the sale of the tangible property. The only question to be answered is the basis for prorating. It seems to us that a fair division would be on the basis of the ratio of the sales price of the tangible property to the total sales price.¹⁵ On the basis of that division, which appears to be equitable, approximately \$19,000 should be charged as a proper expense incurred in connection with the sale of tangible property.

2. Loss on Retirement of DC-4 Non-Rotatable Spare Parts Amounting to \$104,000.

That the loss of \$104,000 on the retirement of DC-4 non-rotatable spare parts is directly related and chargeable to the Route 68 sale transaction is conceded by the Board.¹⁶ The only question raised here is whether the loss on the retirement of the DC-4 non-rotatable spare parts should be charged as an offset against the profit from the tangible property or against the profit from the intangible property. In our opinion, applying the Board's own theory that the profit from the sale of the tangible property should be applied to reduce the amount of the carrier's need for mail pay, it is only fair and equitable that a loss sustained in the retirement of tangible property "related to the operation of Route 68" should be offset against the gain.

Western has been on a permanent rate since January 1, 1949. That rate was established by the Board on the basis of an operation involving only Convair and DC-3 aircraft, equipment, parts, etc. The entire fleet of DC-4's and related parts were disallowed as equipment used and useful in connection with establishing the existing permanent rate

¹⁵ Sales price of tangible property was \$2,250,000 or 3/5ths of the total sales price of \$3,750,000.

¹⁶ Tentative Statement, p. 31; tentative decision pp. 4 and 41, Exhibit PC-43, and statement of Mr. Irons accompanying that exhibit.

effective as of January 1, 1949. So far as the pending proceeding is concerned, December 31, 1948, is the date established for the retirement of DC-4 aircraft and related parts. Although as yet Western has not disposed of its DC-4 fleet, the fact still remains that for the purpose of establishing the rate for the period under review, the Board must proceed on the basis that DC-4 aircraft and parts were retired as of December 31, 1948. To do otherwise would be to ignore the inviolability of the rate review period as announced by the Board in this proceeding. The evidence of record (Tr. pp. 755 and 881) definitely establishes that as of December 31, 1948, Western would have incurred a loss on the retirement of DC-4 non-rotatable spare parts in the amount of \$104,000. As a part of the sale, Western sold several hundred thousand dollars of DC-4 spare parts to

United at a substantial profit, which profit is included 3892 in the net gain on tangible property. It follows that the loss sustained by Western upon the retirement of surplus DC-4 spare parts initially acquired for the operation of Route 68 is properly chargeable against the gain realized from the sale of tangibles in arriving at the net gain or loss from the retirement or sale of tangible property. In holding that the profit from the sale of tangible property should be applied to reduce Western's need, the Board is relying on a line of cases dealing with the retirement of air carrier property. In connection therewith the Board has always followed the policy of considering gains resulting from the normal sale of air carrier property and deducting therefrom losses incurred by the carrier during the same period as the result of the sale or retirement of any such property. The net result, whether it be profit or loss, is considered in connection with establishing the carrier's rate.

The loss on the retirement of DC-4 non-rotatable spare parts is no different from the loss on engine overhaul equipment which the Board in its final decision has properly offset against the profit on the sale of the tangible property.

Both items represent tangible property obtained by the carrier in connection with its operation of Route 68 and which became surplus to the carrier's needs following the transfer to United of Route 68, together with four DC-4's and related equipment, and, therefore, both should be offset against the gain on tangible property.

G. The Board Erred in Adjusting Western's Mail Rate Retroactively to May 1, 1944.

Throughout this proceeding, Western has urged that the Board fix a retroactive mail rate for Western, not 3893 for the entire period May 1, 1944, to December 31, 1948, but for a portion of that period. A cut-off date of January 1, 1946, has been emphasized because that is a significant date in Western's operations during the period in question, contrary to the statement of the Board in its final decision in this case that that date "has no special significance." (p. 12). The factors which demonstrate the importance of that date to Western are set forth in detail at page 20 of Western's brief to the Board, dated March 30, 1950. They need not be repeated here.

In support of a January 1, 1946 date, Western has argued in both of its briefs heretofore filed, in this case—

(1) that the petition which Western filed April 26, 1944, was a limited petition and did not invoke or give the Board jurisdiction to enter upon a general investigation of Western's rates retroactively to that date,

(2) that because the Board has made no finding in this case of excessive earnings in 1944 and 1945 it cannot consider the profits or any part of the profits realized by Western in 1944 and 1945 in determining Western's mail pay requirements for the period in question, and

(3) that as a matter of policy the Board should not recapture mail pay paid to Western under temporary rate orders. The Board has rejected those contentions.

We do not intend to repeat all of the arguments which support Western's position. They are adequately covered

at pages 10-20 of Western's brief filed March 30, 3894 1950, and pages 40-49 of Western's brief filed January 19, 1951.

However, Western does not like to be treated with differently to its detriment. For this reason, it has insisted that the Board is bound to deal with Western as it did with Chicago & Southern in 1948. Chicago & Southern was before the Board in a case which is on all fours factually with this case. *Chicago and Southern Air Lines, Inc., Mail Rates*, 9 C.A.B. 786 (1948). There is no basis on which the two cases can be distinguished. Yet, the Board justifies a "closer scrutiny" of Western's entire rate period on the ground of a change of its policy to embrace what it terms "the better rule." It is difficult to perceive just what was the "rule" which the Board applied in the *Chicago & Southern* case. The decision in that case contains no statement of policy, which the Board need overrule almost three years later.

Equally unconvincing is the Board's attempt to distinguish its holding in *Pan American Grace Airways, Inc., Mail Rates*, 3 C.A.B. 550 (1942). There, the Board decided not to recapture excessive earnings realized by Panagra during the pendency of that rate proceeding, on the ground that the uncertainties of wartime operation as well as the impact of recapture upon everyday business problems of planning and financing in the air transportation field precluded the adoption of a policy which would involve the recapture of those earnings. The Board now says that the effective determinants of its decision in the *Panagra* case were "the fact of total war and the major role of an 3895 international air carrier in that war." The asserted differentiation between "total war" and the present situation in which this country finds itself in Korea and elsewhere is but make-weight argument glossing over the ineptitude with which the Board interprets one of its own decisions. The Board states that Panagra's mail pay was not reduced "because of the uncertainties of wartime opera-

tions as well as . . . [that carrier's] requirements for operating its international routes."

The determinants which the Board in this case finds to have impelled the Board in the *Panagra* case do not comport with what the Board in other cases, following and interpreting the *Panagra* case, has said. In a case decided shortly after the *Panagra* case, Eastern Air Lines was not subjected to recapture even though Eastern had never engaged in the "major role of an international carrier" in World War II. In reviewing Eastern's retroactive mail rates and excessive earnings during the pendency of the proceeding, the Board stated:

"While it is true that the respondent in the *Panagra* case is engaged in foreign air transportation, the Board is convinced that the principal reasons impelling it to decide against recapture of mail compensation in that case are equally applicable in the instant proceeding." *Eastern Air Lines, Inc., Mail Rate Proceeding*, 3 C.A.B. 733, 743 (1942).

On another occasion, called upon to interpret the "recapture" cases, the Board declared:

"We decided that to recapture revenues under those circumstances would be an unsound policy, destructive of stability and confidence in air transportation." *Chicago & Southern Air Lines, Inc., Mail Rates, 1943*, 4 C.A.B. 3896 419 (1943).

Western cannot concede that the considerations recited at pages 564 and 565 of the Board's decision in the *Panagra* case were not "effective determinants" in the refusal to reduce Panagra's rates retroactively.

That January 1, 1946, is a "convenient cut-off date" for Western because prior to that date it earned "substantial profits" which could be screened off from consideration is belabored by the Board. In fact, in the tentative decision in this case, the Board measures the effect of eliminating that portion of the rate period prior to January 1, 1946, at

\$885,000 more mail pay than Western otherwise would be entitled to receive.

However, the prehearing conference report in this case recites the following important issue:

"If, from May 1, 1944, the approximate date of filing of the carrier's petition for a revision of mail rates, to and including December 31, 1945, the carrier received mail compensation at the rate of 60 cents per ton-mile, is the carrier entitled, in the light of the circumstances in this case, to retain all the earnings realized under such rate?"

The Board has failed to resolve this issue, notwithstanding that the 60 cent per ton-mile rate was decreed to be a *service rate* which would compensate the carrier solely for transporting the United States mail. *Western Air Lines, Inc., Mail Rate for Routes 13, 19 and 52*, 4 C.A.B. 441 (1943); *Pennsylvania-Central Airlines Corporation, et al. Motions*, 8 C.A.B. 685, 687 (1947). Until 1946, it is evident that Western was not a "need" carrier. For example, in

the temporary rate order of April 29, 1947, Order, 3897 Serial No. E-484, the Board found, among other things, that "Western's need for mail compensation can be met over a limited period *without any necessity for altering indefinitely its status as a service rate carrier.*"¹⁷ That is, prior to October 1, 1946, according to the Board's findings, Western had no need for subsidy mail pay sufficient to enable it "to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." What was paid to Western on a 60 cent per ton-mile rate represented the judicially determined cost of airmail service, without regard to subsidy. It was the cost to the Post Office Department of service rendered for it by private enterprise. What the Board prophesied in 1943 and 1944 would be the result in

¹⁷ The cited order fixed temporary rates to be used as the basis of payment of mail compensation to Western on and after October 1, 1946.

terms of profit and loss of the application of a 60 cent per ton-mile rate to various carriers, including Western, has been proved by actual experience. Results of operation varied little from the Board's estimates.

Western does not believe that the Board intended to establish a policy in this case which would require in a mail rate proceeding that monies received in payment of the government's obligation to compensate for service rendered on its behalf be offset against "need" requirements of future years. The effect of this would be essentially non-payment or inadequate payment for that service.

However, the Board's decision to review Western's rate to May 1, 1944, has that effect.

Without attributing any inconsistency to the Board's reasoning, because we feel that the Board has not focused on the matter, we call the Board's attention to the following language appearing on page 14 of the final decision in this case:

"It is true . . . that the *non-mail* revenues earned during 1944 and 1945 are included for review with those of 1946, 1947 and 1948 and are balanced against expenses during the entire review period so that the existence of substantial profits in 1944 and 1945 decreases the break-even need which otherwise would result for 1946, 1947 and 1948 alone."

Turning to Appendix No. 1 of the tentative decision in this case, we find that after adjustment by the Board of Western's *reported* break-even need for the last eight months of 1944 and 1945, the "substantial profits" to which the Board has reference amounted to \$96,000 and \$44,000, respectively. A total of \$140,000 is a far cry from the determined excess mail pay received in the 1944 period of approximately \$432,000 and in the year 1945 of approximately \$491,000. The evidence of record in this case discloses that Western received during those periods of time, under the 60 cent per ton-mile rate, mail pay of approximately \$420,000 and \$636,000, respectively. The Board can-

not decrease Western's need in the subsequent years without tapping most, and all in 1944, of that which represented only the cost of air-mail service.

There is no special magic in a January 1, 1946 date. 3899 Western proposed it because, in its opinion, that date reflected a break in the character of Western's operations. Public Counsel suggested that May 1, 1946, was as good a date for cutting off the rate period. We point out that the prehearing conference report leaves open the issue as to whether the Board should fix Western's retroactive rate for the period May 1, 1944, to December 31, 1948, or limit its review to the period January 1, 1946, to December 31, 1948, or "another portion of the period May 1, 1944, to December 31, 1948." *Actually the significant date with respect to Western's operations on a service rate is October 1, 1946, the date on which its status as a service rate carrier first was altered.* According to the Forms 41, during the period May 1, 1944, to October 1, 1946, Western realized, before taxes, a net income of \$315,661, after offsetting losses sustained in the first nine months of 1946 against the profits of 1944 and 1945. The mail pay received during that period on the 60 cent per ton-mile rate and included in arriving at the above-mentioned total net income totalled approximately \$1,314,000.

Western sincerely requests that the Board reconsider fully the effect of its decision as to the rate period. Until 1946, the carrier was self-sufficient, a service-rate carrier. Post-war conditions then compelled the Board to supplement Western's finances by compensation which would permit the carrier to maintain and continue the development of air transportation to the extent and of the character and quality mentioned in the statute. In determining that supplementary need, the Board may not affect what it has determined to constitute the cost of air-mail service.

3900 Notwithstanding, its decision in this case does affect that cost, to the extent that Western in 1944 would receive nothing, and in 1945, 13.68 cents per ton-mile for

carrying the mail. The Board should set aside its ruling as to the rate period and limit the review period in this case to the period either from January 1, 1946, or October 1, 1946, on the one hand, to December 31, 1948, on the other hand.

H. Conclusion

The final decision which the Board adopted on June 26, 1951, has in part corrected the errors contained in its tentative decision adopted on November 24, 1950. This petition affords the Board an opportunity to consider certain new matters as well as to correct errors in its final decision. The Board should reconsider its final decision, and reopen this proceeding, if necessary.

Respectfully submitted,

PAUL E. SULLIVAN

PAUL E. SULLIVAN

Vice President and Secretary

* * * * *

Appendix No. 1

3903

| | | |
|---|-------------------|-------------------|
| 6 | <u>1945</u> | <u>1944</u> |
| - | \$ 148,080.78 | \$ 157,871.88 |
| | (148,080.78) | (157,871.88) |
| | <u> </u> | <u> </u> |
| = | <u><u>-0-</u></u> | <u><u>-0-</u></u> |

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Appendix No. 5

3907

AFFIDAVIT

State of California, County of Los Angeles, ss:

J. Judson Taylor, being first duly sworn, deposes and says:

1. That he is an officer of Western Air Lines, Inc. and holds the position of Treasurer.

2. That in his capacity as Treasurer, he is responsible for and familiar with the preparation of the Company's Federal Income Tax Returns.

3. That as Treasurer, it is his responsibility to approve the payment of such income tax assessments as may be made by the Bureau of Internal Revenue pursuant to their audit of Western's tax returns.

4. That he has prepared the following identified exhibits which he understands will be incorporated as Appendices to Western Air Lines' Petition for Reconsideration to be filed in Docket No. 2870 *et al.*

Appendix No. 1—Western's Actual Tax Liability for the Years 1944 through 1948 as Established by the Bureau of Internal Revenue's audit.

Appendix No. 2—Analysis of Taxable Income as Reported on Western's Federal Income Tax Returns and as Adjusted by Bureau of Internal Revenue for the Years 1944 through 1948.

Appendix No. 3—Western's Actual Tax Liability for the Years 1944 through 1948 on the Basis of Adjustments Made by Bureau of Internal Revenue and Reflecting Final Retroactive Mail Pay Award Per Board Order Serial No. E-5467, dated June 26, 1951.

Appendix No. 4—Analysis of Taxable Income based on Western's Federal Income Tax Returns for the Years 1944 through 1948 as Adjusted by the Bureau of Internal Revenue and Reflecting Final Retroactive Mail Pay Award made by Board Order Serial No. E-5467, dated June 26, 1951.

3908 5. Affiant further states that the information and data contained in Appendices 1, 2, 3 and 4 are true and correct to the best of his information and belief and were obtained from the tax returns filed on behalf of Western Air Lines for the years 1944, 1945, 1946, 1947, and 1948, and from the Bureau of Internal Revenue's Audit Reports dated February 17, 1948, and May 1, 1951, all of which documents he is familiar with, has examined carefully and are available at the Company's General Office, 6060 Avion Drive, Los Angeles 45, California.

6. Affiant further states that the Company has been advised by the United States Treasury Department that on the basis of present returns and audits for the period 1944 through 1948, it will be required to pay Federal income taxes in the amount of \$302,784.52. Additionally, that the Company will be required to pay interest on said tax deficiency in the amount of approximately \$25,000.

7. Affiant further states that tax liability of \$302,784.52 is based on the inclusion as income in 1948 of temporary retroactive mail pay in the amount of \$975,461.20, received in 1949 pursuant to Board Order Serial Nos. E-2531 and E-2506, dated March 3, 1949 and February 25, 1949, respectively.

8. Affiant further states that on the basis of the Board's final decision (Order Serial No. E-5467) and assuming that the excess mail pay per the Board's order is deductible in 1948 for tax purposes, the Company's total taxable net income for the period 1944 through 1948 is \$453,865.10 and its tax liability thereon at the applicable rate of 38% is \$172,468.76. However, if the Company is to retain the fair and reasonable rate which it is entitled to under the Board's final decision that it must be granted additional mail compensation amounting to \$278,175.39 instead of \$172,3909 468.76, the latter amount being subject to income tax.

Furthermore, that the amount of \$278,175.39 is computed as follows:

$$\begin{aligned}
 X &= \text{income tax allowance} \\
 X &= 38\% (\$453,865.10 + X) \\
 X &= \$172,468.76 + .38X \\
 .62X &= \$172,468.76 \\
 X &= \$278,175.39
 \end{aligned}$$

Affiant further states that on the basis of the Board's final decision, Order Serial No. E-5467, dated June 26, 1951, the retroactive mail pay awarded for the period 1944-1948 of \$975,461.20 is reduced to \$632,488.20. Furthermore, that that reduction in taxable income for 1948 will entitle the Company to a refund of part of the tax liability of \$302,784.52, and assuming the Board grants an income tax allowance of \$278,175.39, the amount of tax refund is estimated at approximately \$24,609.13, resulting in a net tax liability to the Company for the period 1944 through 1948, exclusive of estimated interest on tax deficiency, of \$278,175.39.

J. JUDSON TAYLOR

Subscribed and sworn to before me this 20th day of July, 1951

EARNEST H. BROWN

Notary Public in and for the County
of Los Angeles, State of California

My Commission expires December 5, 1952.

3910

Appendix No. 6

AFFIDAVIT

State of California, County of Los Angeles, ss:

Eugene J. Patton, being first duly sworn, deposes and says:

1. That he is manager of the Tax Department of the Los Angeles office, Peat, Marwick, Mitchell & Co., Certified Public Accountants, 618 S. Spring Street, Los Angeles, Calif.
2. That employees in the Los Angeles office of said firm

prepared the Federal corporation income tax returns of Western Air Lines, Inc. for the years 1944 through 1948.

3. That he has reviewed the Revenue Agent's reports; one covering the returns for the years 1944, 1945, and 1946, and one covering the returns for the years 1947 and 1948.

4. That he has reviewed the Appendices referred to in the Affidavit signed by Mr. J. Judson Taylor, Treasurer of Western Air Lines, dated July 20, 1951, and finds that the data and information contained in Appendices 1 through 4 are true and correct.

5. That the Federal corporation tax liability of Western Air Lines, Inc., in the aggregate for the years 1944 through 1948, on the basis of the corporation's Federal tax returns as adjusted by the Revenue Agent's examinations referred to above, is \$302,784.52.

6. That assuming the excess mail pay per the Board's final decision (Order Serial No. E-5467, dated June 26, 1951) in the amount of \$342,973 is deductible for Federal income tax purposes in 1948, the tax liability in the aggregate for the years 1944 through 1948 will be \$172,468.76, as indicated in Appendix No. 3 and referred to in Mr. J. J. Taylor's affidavit.

EUGENE J. PATTON

Subscribed and sworn to before me this 24th day of July, 1951.

LILLIAN H. TRYON
Notary Public

My Commission expires February 5, 1954.

* * * * *

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

ADOPTED BY THE CIVIL AERONAUTICS BOARD
AT ITS OFFICE IN WASHINGTON, D. C.
ON THE 12TH DAY OF OCTOBER, 1951.

Docket No. 2870 *et al.*

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, of

INLAND AIR LINES, INC.

over its entire system, and of

WESTERN AIR LINES, INC.

over its routes within the continental United States insofar as authorized under its certificates for interstate air transportation and over its routes between the United States and terminal points in Canada.

Opinion and Order on Petition for Reconsideration

On June 26, 1951, the Board issued its final opinion and order¹ disposing of exceptions to its tentative decision in this proceeding and fixing final rates of compensation for the transportation of mail by Western Air Lines, Inc. (hereinafter called Western), and Inland Air Lines, Inc. (hereinafter called Inland), covering the period May 1, 1944 through December 31, 1948, for Western, and the period March 28, 1947 through December 31, 1948, for In-
3915 land.

On August 1, 1951, Western filed a petition for rehearing, reargument, and reconsideration of this opinion and order which was directed in large part to the dollar amount of the allowance for Federal income taxes in the

¹ Order Serial No. E-5467.

mail rate. The Postmaster General also filed a petition for reconsideration on July 27, 1951, objecting to that portion of the decision which permitted Western to retain the profit on the intangibles realized from the sale of Route No. 68.

Applying the tax return technique, we made no provision in the final decision for Federal income taxes for Western since, on the state of the record, Western had no tax liability. Although counsel for Western stated at the oral argument on exceptions to the tentative decision that as a result of an audit by the Bureau of Internal Revenue there was a basis for a tax allowance, we did not receive the evidence related to the tax claim until Western filed its petition for reconsideration.

Western now claims that its tax liability amounts to \$278,175, and requests that provision be made therefor in its mail rate. This new claim does not arise principally from newly discovered facts. It appears to be based for the most part on Western's assumption that the mail rate should include an allowance for taxes on the profit from the sale of the route which we did not use as "other revenue" to reduce the carrier's "need."

The only new matter regarding Western's tax liability is the fact, set forth in affidavits accompanying the petition, that the Bureau of Internal Revenue has allowed Western to defer \$118,832 of Convair training expenses to be amortized over future years, rather than treating this item as a charge to expense in the year 1948. Since Western was obviously aware of this adjustment to its 1948 income tax return prior to the oral argument on May 21, 1951, the

3916 carrier should have provided this information for the record in time to permit its consideration in our final decision. Without this change reflected in Western's income tax return, it appeared at the time of the final decision that Western had no tax liability whatsoever. The withholding of this information from formal introduction into the record until this late date cannot be justified. Such action merely hampered the Board in the disposition of the

case. While we have considered this newly introduced data, we have done so only because we do not wish to penalize the carrier. However, we will not sanction such a procedure in future cases.

According to Appendix 4 of Western's petition, its net taxable income as adjusted for the period under review and for the amount of mail pay we allowed in the final decision is \$453,865. However, this amount includes that part of the revenue from the sale of Route No. 68 which we decided should not be regarded as "other revenue". Accordingly, we are not required to provide for the taxes which are related to this revenue. After deduction of this profit from the net taxable income there is a balance of only \$6,865 which may be considered as taxable income for rate-making purposes. The income tax on this amount at a rate of 38 percent would be \$2,609. However, the latter amount would itself be included as gross income and be taxable accordingly. Therefore, in order to provide Western with sufficient funds to pay the tax on this amount of net taxable income including all the mail pay due as a result, it is necessary to increase the allowance for taxes to \$4,208.

Western also claims that the Board should have reduced by an additional \$123,000 the profit from the sale of Route No. 68 which was taken as an offset against "need." This amount represents the larger part of certain claimed 3917 miscellaneous expenses related to the sale of the route, and an estimated \$104,000 loss on the retirement of DC-4 non-rotatable spare parts.

In our final decision we held that since Western was to keep the profit from the sale of intangible property, no question of offsets against Western's net profit on intangibles was involved. Now, Western argues that \$104,000, the amount of the estimated loss on retirement of DC-4 non-rotatable spare parts, should be charged against the profit from the sale of the tangible property. However, we find, on re-examining the nature of this allowance, that Western's contention must be denied.

It is clear that the \$104,000 amount we recognized as the estimated loss as of December 31, 1948, was an allowance in the nature of a reserve for a possible loss. The fact is, however, as Western admits in its petition for reconsideration, that the carrier has still not disposed of its DC-4 fleet. It does not deny that it has been able to use the spare parts for almost three years since December 31, 1948, nor does it assert that an actual loss was incurred. Moreover, it is common knowledge that during the present emergency aircraft materials and parts are in short supply and that there has been a substantial increment in their value. In any event, it appears that any loss actually incurred would easily be compensated for by the reserve of \$200,000 Western was allowed to accrue against the estimated loss on DC-4 non-rotatable spare parts during the period ended December 31, 1948.

Western contends that it should be permitted to charge \$19,000, or three-fifths of the so-called miscellaneous expenses of \$32,389, against the profit from the sale of the tangible property. The carrier arrived at this \$19,000 figure by making an allocation on the basis of the ratio of the sales price of the tangible property to the total sales price of the route. Since there is no evidence that the claimed miscellaneous expenses were incurred in proportion to the sales value of the respective kinds of property, we cannot accept the proposed allocation.

The carrier apparently suggests this allocation because it has been able to identify no more than \$3,898 of the total claimed charges as expenses resulting from the transfer of the tangible property. It should be pointed out that this rather superficial breakdown was presented for the first time in the petition for reconsideration of our final opinion. The carrier has thus had an opportunity to proffer any available evidence it may have as to the charges allegedly incurred against the profit from the sale of the tangible property. We are satisfied that a charge of not more than \$3,898 appears to be warranted against the net profit from

the sale of the tangibles involved in the transfer of Route No. 68.²

Careful review of all other matters raised in Western's petition discloses that they involve no facts or considerations in addition to those fully considered by us in the final decision and do not warrant any further change in that decision. We have also fully considered the contentions in the Postmaster General's petition for reconsideration and find they do not justify modification of our prior determinations. Western's request for further hearing and argument is without merit, particularly since the Board has now had the benefit of three separate briefs by Western, its newly filed affidavits, and oral argument on two occasions. Therefore, except to the extent granted herein, the petitions of both the Postmaster General and Western are denied.

In view of the foregoing revision of our final decision, we find, as detailed in Appendix I, that Western is entitled to receive total final mail pay of \$3,917,361. Since Western has received temporary mail pay of \$4,252,000 for operations during the period under review, we now find that the carrier has received an overpayment of \$334,639.

Accordingly, IT IS ORDERED THAT:

1. Insofar as the opinion accompanying Order Serial No. E-5467, adopted June 26, 1951, is inconsistent with the find-

² The effect of allowing this offset is to increase from \$4,208 to \$4,295 the allowance for Federal income taxes computed on the basis of Western's tax return, discussed *supra* page 2. The amount of the increase is determined as follows:

| | |
|--|-----------|
| Net taxable income claimed by Western | \$453,865 |
| Mail pay required by offset against profit from tangibles (moving and storage charges) | 3,898 |
| Increase in return to reflect inclusion of additional mail pay in recognized investment | 141 |
| | <hr/> |
| | \$457,904 |
| Deduct net taxable income not recognized for rate-making purposes | 450,898 |
| | <hr/> |
| Net taxable income recognized for rate-making purposes | \$ 7,006 |
| Allowance for Federal income taxes at a rate of 38% | \$ 4,295 |

ings made herein the opinion shall be, and it is, hereby modified in accordance with the said findings.

2. The first part of the second ordering paragraph of Order Serial No. E-5467, adopted June 26, 1951, be, and it is, hereby amended in its entirety to read as follows:

IT IS ORDERED, That the fair and reasonable final rate of compensation to be paid Western Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its routes within the continental United States insofar as authorized by its certificates of public convenience and necessity for interstate air transportation and over its routes between the United States and terminal points in Canada, for the period May 1, 1944-December 31, 1948, inclusive, is hereby fixed, determined, and published to be the amount of \$3,917,361.

3920 3. Except to the extent granted herein, the petition for reconsideration of Western be, and it is, hereby denied.

4. The petition of the Postmaster General for reconsideration be, and it is, hereby denied.

Nyrop, Chairman, Ryan, Lee, Adams, and Gurney, Members of the Board, concurred in the above opinion and order.

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

(SEAL)

3921

Appendix I*Computation of Total Mail Pay Due Western*

| | | |
|--|-----------|--------------------|
| Mail pay awarded in final opinion | | <u>\$3,909,027</u> |
| Net profit on tangible property as found in final opinion | \$652,000 | |
| Net profit on tangible property after offset of moving and storage expense (\$3,898) | 648,102 | 3,898 |
| Increase in break-even need owing to offset | | 141 |
| Increase in return to reflect added mail pay in recognized investment | | <u>4,295</u> |
| Allowance for Federal income taxes | | <u>\$ 8,334</u> |
| Total increase in mail pay | | <u>\$3,917,361</u> |
| Total mail pay due Western | | |

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[fol. 340] [File endorsement omitted]

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT
OF COLUMBIA CIRCUIT

No. 11,259

JESSE M. DONALDSON, Postmaster General of the United
States, and THE UNITED STATES OF AMERICA, on behalf of
the Postmaster General, PETITIONERS,

v.

CIVIL AERONAUTICS BOARD.

Before: Edgerton, Acting Chief Judge, in Chambers.

ORDER ALLOWING SUBSTITUTION OF PARTY PETITIONER—FILED
FEBRUARY 25, 1953.

Upon consideration of the motion of petitioners for leave to substitute Arthur E. Summerfield, Postmaster General of the United States as a party to this action on the ground that Jesse M. Donaldson has resigned from the office of Postmaster General of the United States and that Arthur E. Summerfield, having been duly appointed as successor to Jesse M. Donaldson, is now lawfully acting as Postmaster General of the United States, and it having been alleged that there is substantial need for continuing and maintaining this action, and it appearing that the respondent has not filed objections thereto, it is

Ordered that the motion be granted and that Arthur E. Summerfield, Postmaster General of the United States, be, and he is hereby, substituted in the place and stead of Jesse M. Donaldson as petitioner.

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United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 11259

ARTHUR E. SUMMERFIELD, Postmaster General of the United States, and THE UNITED STATES OF AMERICA, on behalf of the Postmaster General, PETITIONERS

v.

CIVIL AERONAUTICS BOARD, RESPONDENT

No. 11324

WESTERN AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD, RESPONDENT

On Petitions for Review of Orders of the
Civil Aeronautics Board

Decided May 4, 1953

Mr. Daniel M. Friedman, Special Assistant to the Attorney General, Department of Justice, *pro hac vice*, by special leave of Court, with whom *Mr. Newell A. Clapp*, Acting Assistant Attorney General, Department of Justice, was on the brief, for petitioners in No. 11259. *Mr. Charles H. Weston*, Chief, Appellate Section of the Anti-

trust Division, Department of Justice, and *Mr. William E. Kirk, Jr.*, Assistant United States Attorney at the time of argument, also entered appearances in behalf of the petitioners in No. 11259.

Mr. Hugh W. Darling for petitioner in No. 11324. *Mr. L. Welch Pogue* also entered an appearance in behalf of petitioner in No. 11324.

Mr. O. D. Ozment, Attorney, Civil Aeronautics Board, with whom *Mr. Emory T. Nunneley, Jr.*, General Counsel, Civil Aeronautics Board, was on the brief, for respondent. *Mr. John H. Wanner*, Associate General Counsel, Civil Aeronautics Board, also entered an appearance in behalf of respondent.

Before PRETTYMAN, PROCTOR and BAZELON, Circuit Judges.

PRETTYMAN, *Circuit Judge*: These cases concern orders of the Civil Aeronautics Board which fixed the compensation of Western Air Lines for the transportation of mail from May, 1944, through December, 1948. The dispute revolves about Section 406 of the Civil Aeronautics Act.¹ The proper treatment of several matters is involved.

Principally the petitions concern the treatment of the profit derived by Western from the sale to United Air Lines of a certificate for an air route and certain equipment used in connection therewith. Prior to September 15, 1947, Western owned a certificate for Route 68—between Los Angeles and Denver. After a hearing the Civil Aeronautics Board approved the sale of the route and the equipment to United Air Lines² for a total price of \$3,750,000. Of this \$722,000³ was then computed as

¹ 52 STAT. 998 (1938), as amended, 49 U.S.C.A. § 486.

² United-Western, Acquisition Air Carrier Property, 8 C.A.B. 298 (1947).

³ Later recomputed to be \$648,102.

profit on the sale of tangibles and \$447,000 as profit on the sale of intangibles. The Board decided that the transfer of the route at the amount to be paid by United was in the public interest, because the profit on the transaction would provide the necessary incentive for Western to make a sale and the purchasing carrier could operate the property to greater advantage to the public. The Board acted upon the premise that it has no power to force a carrier against its will to transfer property to another carrier; its only power to influence such transfers is the power of inducement. It decided that a profit on a sale would be such an inducement. Hence it approved the sale.

When the Board came, in the present proceeding, to the determination of compensation to Western for the transportation of mail, a problem arose as to the treatment of this profit in the computations.

The statute, in pertinent part, provides:

“(a) The Board is empowered and directed * * * to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft * * *

“(b) * * * In determining the rate in each case, the Board shall take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.”⁴

⁴ *Supra* note 1.

The statutory language which is critical in the present dispute is "the need of each such air carrier for compensation * * * sufficient * * *, together with all other revenue of the air carrier, * * * to maintain and continue the development of air transportation".⁵

Perhaps the problem is made clearer by use of a little simple arithmetic. If a carrier has \$1,000,000 in revenue and \$1,300,000 in expenses, obviously it needs \$300,000 to break even; the "break even need". Then it needs a return on its investment and some working capital; let us say \$200,000 for those needs. The statute says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation. Let us suppose that for the latter purpose the carrier needs another \$100,000. In sum the carrier needs \$600,000. Now, obviously, in this calculation the greater the amount of the carrier's existing revenues, the less the amount it needs by way of additional mail pay; and the less the revenues the greater the additional mail pay. So the inclusion of a given amount in revenues lessens the mail pay by that amount, and the omission of an amount from revenues increases the needed mail pay. Such is our present problem.

The Board at first decided that the entire profit on the sale of Route 68 was "other revenue", and it included this amount as revenue in calculating the amount of mail pay needed by Western. The effect was to reduce the mail pay by that amount. Upon reconsideration the Board changed its position. It included the profit from the sale of tangibles as "other revenue" in its calculation, but it did not include the profit from the sale of intangibles. The effect was to reduce mail pay by the amount

⁵ Of course the statute provides, in effect, for a minimum which is actual compensation for service performed. That payment is not in dispute here.

of the profit on the tangibles, but the profit on the intangibles was left out of the calculation entirely.

The Postmaster General is a party in interest by reason of the duties in respect to mail pay imposed upon him by the statute.⁶ He says the Board was in error in its treatment of the profit on the intangibles. Western says the Board was in error in its treatment of the profit on the tangibles. The Postmaster General would include in revenues the entire profit on the sale of the route and the equipment. Western would exclude the entire profit from revenues in the calculation.

We turn first to the problem of the profit on the tangibles. This was a gain derived from the sale of capital assets. As such it was "income" within the meaning which that term has had ever since *Doyle v. Mitchell Bros. Co.*⁷ But our problem is whether it was "revenue" within the meaning of this rate-making statute. We think the answer should be sought chiefly in the substantive meanings of the statutory provisions rather than in the semantics of the phrases.

The difficulty of the problem arises because this proceeding is to determine a rate of compensation for a past period. Ordinarily, of course, rates are fixed for the future. We think it clear that the profit from an isolated past sale of capital assets could not be included in a calculation of compensation to be paid in future years for carriage of the mail. It would not be anticipated revenue in the future period. With that proposition the Board agrees. In fixing the rate for the future it has considered as revenue only reasonably anticipated items.

Western bases its foremost argument upon the foregoing as a premise. It insists that the present proceeding is a rate-making proceeding and nothing else; that a rate-

⁶ Sec. 406 of the Act, 52 STAT. 998 (1938), 49 U.S.C.A. § 486.

⁷ 247 U.S. 179, 62 L.Ed. 1054, 38 S.Ct. 467 (1918).

making proceeding must be, in contemplation of law, rate-making for the future—a prospective rate-making, since, it says, rate-making is inherently a prospective concept. The Board itself has several times so held. And, of course, that is a generally accepted view as to utility rates. There is great power in that argument.

But we are impressed by the practical aspects of the situation. In this instance the Board was in fact looking at a period which had passed. The actual facts as to revenues and expenses for that period were known. The actual need, or lack of it, of the carrier in that period was known. In saying that the Board was looking at a past period we are not departing from the rule in the *T. W. A.* case.⁸ The period began when the petition for the rate-making was filed, *i.e.*, May, 1944; as of that date the rate-making was prospective. When the Board got around to making its findings and decision the period 1944-1948 was past. It is to the latter actuality that we refer.

At this point the two different considerations embodied in this statute must be noted. The statute provides for actual compensation for the service performed in carrying the mail—a so-called service rate. This is the ordinary purpose of a utility rate. It involves reimbursement for expenses incurred in performing the service, return on the investment used in the service, and a reasonable profit on the transaction. This much is due whether the service is past or future. In the case at bar no dispute arises in respect to that phase of the matter.

But this statute adds to these ordinary features of a utility rate another consideration. It provides that the pay for carrying the mail shall be sufficient to meet the carrier's need. It describes that need as being for funds to perform the service of carrying the mail and also to maintain and develop air transportation. The problem

⁸ *T. W. A. v. Civil Aeronautics Board*, 336 U.S. 601, 93 L.Ed. 911, 69 S.Ct. 756 (1949).

under this provision of the statute is: How much does the carrier need? The answer depends upon (1) the gross, or total, need in dollars and (2) how much the carrier will have outside of mail pay.

In the ordinary case, where the rates are for the future, the revenue of the carrier must be anticipated. But where the pay is being computed for a past period may the Board accept as a fact that which it knows to be a fact, or must it ignore the known fact and compute the rate as though it were looking at the unknown future as of the date of the beginning of the period? The Board knew, and we all know, that Western had in this period this \$1,000,000, or thereabouts, in profit. That profit was derived from the disposition of assets acquired for or created by its operations under its certificate.

Let us suppose, as was the case in the basic findings here, that Western's total non-mail revenue was about \$33,000,000 and its total operating expenses were about \$36,000,000. How much does it need? How much does it need if, in addition to the \$33,000,000, it also has a special profit of \$1,000,000? Does it actually need \$3,000,000, or does it actually need only \$2,000,000?

The gist of the answer lies in the fact that we are to determine "need". We are not determining merely adequate compensation for services rendered, in the ordinary public utility sense. To be sure, the payment is cast by the statute as a rate, and the process as a rate-making. But even so the Supreme Court held in the *West Ohio Gas* case⁹ that, when the period under consideration has passed, fair and reasonable rates should be ascertained from what is known and not from a *nunc pro tunc* estimate. In the case now before us the disputed basic consideration is a need, a need beyond the requirements of fair compensation for a service performed, not dependent

⁹ *West Ohio Gas Co. v. Comm'n* (No. 2), 294 U.S. 79, 82, 79 L.Ed. 773, 55 S.Ct. 324 (1935).

upon the amount or the nature of the service rendered. *A fortiori*, from the *West Ohio Gas* case, the amount of need for a period which has passed must be ascertained in the light of known facts.

It seems to us that under this statute the Board, in fixing a rate of compensation for a past period, may view the facts as it knows the facts to be, that in determining "need" it is not compelled to ignore that which it knows. We conclude that in ascertaining Western's need for the period May, 1944, to December, 1948, the Board was permitted to take into consideration the fact that Western had this profit in that period from the sale of these assets.

We fully realize that our view of the statute will give rise to difficulties in respect to losses and also in respect to unusual or unanticipated earnings. The rule may make too much depend, from the standpoint of the carrier, upon tactical decisions whether and when to file petitions for rate-making. But we think such possibilities cannot negative statutory terms. Moreover other difficulties arise from any other rule. And, again, it seems to us that much of the anticipated difficulty can be prevented by expedition on the part of the Board, so that what is prospective in legal theory will be prospective in actual fact. If expeditious disposition of petitions does not meet the troubles arising from the rule, it is always possible that Congress may change the statutory provision. Our part is done when we conclude what Congress meant by the provision now before us.

We turn next to the treatment of the profit on the intangibles. The Board did not find, and it does not claim now, that Western itself needs the additional amount of mail pay which is shown when the profit on the sale of the intangibles in this transaction is omitted from "other revenue" in the computation. The claim of the Board is that it can allow Western to exclude this sum from stated revenues in order to encourage other carriers (not West-

ern) to follow a given course of action. The Board said, in its opinion in the present case, that it wished to emphasize that the "decision not to include the net profit from the sale of intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers. In other words, we have decided not to offset this profit against the carrier's need because we are seeking in this way to spur the development of a self-sufficient air transport industry."

We recognize the force of the Board's description of the desirability of encouraging carriers to transfer routes and other property. But we cannot find in the statute any power conferred upon the Board to do so in fixing mail pay. We do not find any mail pay provision which is authority for the Board to provide incentives to the industry generally for the development of air transportation through the voluntary actions of carriers.

In the first place, the language of the statute sharply limits developmental allowances to the needs of the carrier under consideration. (1) The statute speaks of the "need" of the carrier. It does not speak of the desirability of allowances. It does not speak of purely bonus awards. (2) It speaks of "each" air carrier and compensation sufficient to enable "such air carrier" to develop. The statute is not cast in terms applicable to the general field of air transportation but to the situation in which each air carrier finds itself. (3) The statute provides that the mail pay shall be sufficient "to enable" the air carrier to maintain and continue development. This is a sharply limited expression. It does not extend to bonus awards which might be encouraging to the industry generally. Thus we think that, while the so-called "need" provision of the statute, above quoted, does provide for the payment of sums sufficient to enable the carrier under consideration to maintain and continue development of air transportation, such payments are restricted to the need

of each individual carrier to maintain and continue a development program of its own.

In the second place, the Supreme Court held in the *T. W. A.* case, *supra*, that the mail pay provisions of this statute describe a rate-making authority, and the Court said that the statutory language does not suggest that Congress intended to break with the traditions of public utility rate-making. Allowances designed as developmental incentives for the utility whose rates are being determined are quite common in public utility rate-making. But the award of bonus subsidies for the purpose of encouraging an industry generally to follow courses deemed desirable by the regulatory authority is a vast departure from rate-making. Mr. Justice Jackson made this distinction indisputably clear in his dissent in the *T. W. A.* case. He was of opinion that in these provisions of the statute Congress intended to subsidize the carriers and to underwrite their revenues. We think that the decision in the *T. W. A.* case as to the nature of the mail pay provisions leaves no room for bonus subsidies not connected with the particular carrier's own need. So the statute does not support the theory upon which the Board desires to go in this proceeding in respect to the profit from the intangibles.

We must conclude, therefore, on this point that the Board was in error in the theory upon which it excluded from the calculation the profit from the sale of the intangibles.

The parties dispute the Board's treatment of federal income tax liabilities in its computation of the mail pay. The tax liability upon an estimated basis as of the beginning of the period was some \$600,000. It developed that, due to carry-back losses and other provisions of the federal tax statutes, Western had little or no tax liability for this period. In its final orders on mail pay the Board acted upon the latter basis of fact. We think it was

correct in doing so. The preceding discussion is sufficient as a statement of our reasons.

Western also asserts that the Board erred in including as "other revenue" in the calculation of mail pay the profits derived from the operation of restaurants and slot machine concessions at its airports. We think the Board was clearly correct in this treatment. When the statute says "all other revenue" it must mean to include revenue derived from activities incidental to the operation of the airline. Whether it would also include revenue from activities unconnected with airplane operation is a question not before us and upon which we intimate no opinion.

Western asserts as reversible error the decision of the Board to fix in this proceeding the mail pay beginning in May, 1944. Western says that the consideration should have begun as of January 1, 1946. But the Board has power under the statute (Sec. 406(a)) to "make such rates effective from such date as it shall determine to be proper", and the Supreme Court held in the *T. W. A.* case that that clause empowered the Board to go back as far as the date of the filing of the petition. That is what the Board did in this case. Western filed its petition for redetermination of mail pay on May 1, 1944.

We add one further comment in regard to the expressions "offset", "deduction" and "recapture" used by the parties in describing the treatment of the profit from the sale of the assets if it be included in revenue. The phraseology would not be important if it did not embody erroneous ideas. The need which this statute contemplates is a net figure; the extra amount which appears necessary over and above that which the carrier has. The process provided by the statute is for an affirmative ascertainment of that need. The need is not a gross figure from which offsets or deductions are made. Thus the passenger revenue, etc., is not "offset" against or "deducted" from the need of the carrier. None of the earned revenue is recaptured. The bare, uncomplicated

situation is that when the carrier has substantial revenues from non-mail sources the margin of its need for mail pay is less. In practical dollar effect, and perhaps in accounting entries, the treatment may be set up as a gross need with offsetting items, and so it takes on an appearance of recapture. But the legal contemplation of the statute is not that, and the use of the quoted terms leads to erroneous reasoning.

The necessity for reconsiderations, redeterminations and recalculations in the light of this opinion causes us to remand the matter to the Board. The remand is to enable the Board to determine, in the light of this opinion and pursuant to the statutory terms, the amount of compensation to be paid Western for the transportation of mail during the period here involved—May, 1944, to December, 1948.

Affirmed in part, reversed in part, and remanded.

BAZELON, *Circuit Judge*, concurring: I agree with the court's opinion and its comment that the rule we adopt in construing the statute "will give rise to difficulties in respect to losses and also in respect to unusual or unanticipated earnings"¹ but I am unable to agree that "much of the anticipated difficulty can be prevented by expedition on the part of the Board."² I think these difficulties or "other difficulties [which might] arise from any other rule"³ are inherent in the statute and will persist so long as there is no express differentiation therein between compensation for mail service and need payments to subsidize the development of air transportation. This is

¹ Majority opinion, p. 8.

² *Ibid.*

³ *Ibid.*

so because the absence of such a distinction, says the Supreme Court, requires the application of traditional principles of rate making.⁴ The effect of this is to make applicable to subsidy as well as compensation payments the familiar principle that "past excessive earnings belong to the [carrier] just as past losses must be borne by it."⁵ Therein lies the mischief. For that principle derives its validity from the premise that rates are calculated to allow for some financial risk on the part of the public utility.⁶ But since the very purpose of need or subsidy payments is to remove any vestige of risk, that principle has no place in fixing such non-rate payments.

⁴ Transcontinental & Western Air v. Civil Aeronautics Board, 336 U.S. 601, 605 (1949).

⁵ Washington Gas Light Co. v. Baker, 88 U.S.App.D.C. 115, 125, 188 F.2d 11, 21 (1950), *cert. denied*, 340 U.S. 952 (1951). And see my concurrence this day in Summerfield, et al. v. Civil Aeronautics Board, No. 11351.

⁶ *Ibid*, and cases cited in note 15 therein.

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[fol. 354]

[File endorsement omitted]

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT
OF COLUMBIA CIRCUIT

No. 11,259

ARTHUR E. SUMMERFIELD, Postmaster General of the United
States, and THE UNITED STATES OF AMERICA, on behalf of
the Postmaster General, PETITIONERS,*v.*

CIVIL AERONAUTICS BOARD,

No. 11,324

WESTERN AIR LINES, INC., PETITIONER,

v.

CIVIL AERONAUTICS BOARD,

On Petitions for Review of Orders of the Civil Aeronautics
Board.

Before: Prettyman, Proctor and Bazelon, Circuit Judges.

JUDGMENT AND DECREE—FILED MAY 4, 1953

These cases came on to be heard on the transcript of the record from the Civil Aeronautics Board, and were argued by counsel.

On consideration whereof, it is adjudged and decreed by this Court that the orders of the Civil Aeronautics Board on review in these cases be, and the same are hereby, affirmed in part and reversed in part, and that these cases be, and they are hereby, remanded to the said Civil Aeronautics Board for further proceedings in conformity with the opinion of this Court.

Per Circuit Judge Prettyman.

Separate concurring opinion by Circuit Judge Bazelon.

[fol. 355]

[File endorsement omitted]

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT
OF COLUMBIA CIRCUIT

No. 11,259

[Title omitted]

No. 11,324

[Title omitted]

Before: Wilbur K. Miller, Circuit Judge, in Chambers.

ORDER ALLOWING CONSOLIDATION OF CASES—FILED MARCH
22, 1952.

Upon consideration of the joint motion of all of the parties herein to consolidate the above-entitled cases for the filing of briefs, for hearing and for decision and to extend the time for filing petitioners' briefs and the joint appendices to and including April 23, 1952, it is

Ordered that the motion be, and it is hereby granted.

[fol. 356]

[File endorsement omitted]

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT
OF COLUMBIA CIRCUIT

Nos. 11259 and 11324

[Title omitted]

DESIGNATION OF RECORD—FILED JUNE 15, 1953.

The Clerk will please prepare a certified transcript of record for use on petitions to the Supreme Court of the United States for writs of certiorari in the above-entitled consolidated case, and include therein the following:

1. Joint Appendix to briefs.
2. Order consolidating Case Nos. 11259 and 11324 for hearing and decision.

3. Order substituting Arthur E. Summerfield, Postmaster General, as a petitioner in Case No. 11259 in lieu of Jesse M. Donaldson, former Postmaster General.

4. Opinion.

5. Judgment.

6. This designation.

7. Clerk's certificate.

(S.) L. Welch Pogue, Attorney for Western Air Lines,
Inc. (S.) Emory T. Nunneley, Jr., General Counsel,
Civil Aeronautics Board.

[fol. 357] Receipt of the foregoing Designation of Record is hereby acknowledged, and no counter-designations will be made on behalf of Summerfield, *et al.*

(S.) Charles H. Weston, Chief, Appellate Section,
Antitrust Division, Department of Justice, Attor-
ney for Summerfield, *et al.*

[fol. 358] Clerk's Certificate to foregoing transcript omitted in printing.

(9113)

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[fols. 357-358] SUPREME COURT OF THE UNITED STATES,

OCTOBER TERM, 1953

No. 224

CIVIL AERONAUTICS BOARD, Petitioner

vs.

ARTHUR E. SUMMERFIELD, Postmaster General of the United States of America, on Behalf of the Postmaster General and Western Air Lines, Inc.

ORDER ALLOWING CERTIORARI—Filed October 12, 1953

The petition herein for a writ of certiorari to the United States Court of Appeals for the District of Columbia Circuit is granted. The case is consolidated for argument with Nos. 222, 223, and 225.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

The Chief Justice took no part in the consideration or decision of this application.

[fols. 359-360] SUPREME COURT OF THE UNITED STATES,
OCTOBER TERM, 1953

No. 225

WESTERN AIR LINES, INC., Petitioner,

vs.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMERFIELD, Postmaster General of the United States, and the United States of America, on Behalf of the Postmaster General

ORDER ALLOWING CERTIORARI—Filed October 12, 1953

The petition herein for a writ of certiorari to the United States Court of Appeals for the District of Columbia Cir-

cuit is granted. The case is consolidated for argument with Nos. 222, 223, and 224.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

The Chief Justice took no part in the consideration or decision of this application.

(1111)

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(I)

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. —

CIVIL AERONAUTICS BOARD, PETITIONER

v.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL
OF THE UNITED STATES; THE UNITED STATES OF
AMERICA, ON BEHALF OF THE POSTMASTER GEN-
ERAL; AND WESTERN AIR LINES, INC.

*PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES COURT OF APPEALS FOR THE DISTRICT OF
COLUMBIA CIRCUIT*

The Civil Aeronautics Board respectfully prays that a writ of certiorari be issued to review that portion of the judgment of the United States Court of Appeals for the District of Columbia Circuit, entered in the above-entitled consolidated case on May 4, 1953, which reversed in part the order of the Civil Aeronautics Board under review.

OPINION BELOW

The opinion of the Court of Appeals for the District of Columbia Circuit (R. 341) is not yet reported. The orders and findings of the Civil Aeronautics Board (R. 183, 258, 333) are not yet reported.

(1)

JURISDICTION

The judgment of the Court of Appeals was entered on May 4, 1953 (R. 354). The jurisdiction of this Court is invoked under Title 28, United States Code, Section 1254 (1).

QUESTIONS PRESENTED

1. Whether, after having approved the purchase price to be paid by an air carrier for one of the air routes of another as being in the public interest because the profit to the selling carrier would provide the incentive for the sale, the Civil Aeronautics Board, in fixing a "fair and reasonable" need mail rate for the selling carrier, was required by Section 406 of the Civil Aeronautics Act to reduce, by the amount of profit attributable to the sale of the route, the mail pay allowance to which the carrier otherwise was entitled.

2. Whether the provisions of Section 406 of the Civil Aeronautics Act preclude the Civil Aeronautics Board from declining, as a matter of regulatory policy and for the purpose of encouraging voluntary route transfers deemed necessary in the public interest, to reduce need mail rates otherwise "fair and reasonable" by the amount of profits derived from route sales.

STATUTE INVOLVED

The pertinent provisions of the Civil Aeronautics Act, which will be referred to as the Act, are set forth in the Appendix, *infra*, pp. 16-18.

STATEMENT

This case arises out of a proceeding before the Civil Aeronautics Board in which a final air mail rate was fixed for Western Air Lines, Inc. for the past period May 1, 1944–December 31, 1948. Both the Postmaster General and Western were parties to the Board's proceeding, and both sought review of the Board's order. The petitions for review were consolidated for hearing and **decision** by the Court of Appeals (R. 355), and a single opinion and judgment was entered (R. 341, 354). The Court of Appeals affirmed the Board's order insofar as it was challenged by Western (Case No. 11324 below), and reversed the order in part upon the basis of the challenge made by the Postmaster General (Case No. 11259 below). The facts pertinent to this petition and the partial reversal of the Board's order follow.¹

In 1947, Western entered into a contract with United Air Lines for the sale, at a profit in excess of \$1,000,000, of Western's certificate and properties for air operations between Los Angeles and Denver (Route 68). After imposing appropriate conditions to insure that the portion of the purchase price paid by United in excess of the actual value of the physical assets would not

¹ Western also has filed a petition for the issuance of a writ of certiorari to review the judgment below. *Western Air Lines, Inc. v. Summerfield et al. and the Civil Aeronautics Board*, this term.

be recouped by United from either the public or the Government, the Board approved the sale of the *United-Western, Acquisition of Air Carrier Property*, 8 C. A. B. 298. As stated by the Court of Appeals (R. 343):

The Board decided that the transfer of the route at the amount to be paid by United was in the public interest, because the profit on the transaction would provide the necessary incentive for Western to make a sale and the purchasing carrier could operate the property to greater advantage to the public. The Board acted upon the premise that it has no power to force a carrier against its will to transfer property to another carrier; its only power to influence such transfers is the power of inducement. It decided that a profit on a sale would be such an inducement. Hence it approved the sale.

At the time of the approval of the sale, Western was conducting operations under a temporary "need" or subsidy mail rate (R. 44), having petitioned the Board in April, 1944 for the fixing of a need rate to be made effective from May 1, 1944 (R. 15). Subsequently, on December 30, 1948, the Board proposed a final lump sum need payment for operations over Western's entire air carrier system for the past period May 1, 1944-December 31, 1948, and a need rate for the future (R. 54). Only the lump sum payment for the past period is here in issue.

Section 406 (b) of the Act (*infra*, p. 18) provides in part that, in fixing "fair and reasonable" mail rates, the Board "shall take into consideration, among other factors," the "need" of the carrier for mail compensation, which, "together with all other revenue of the air carrier," will enable the carrier to "maintain and continue the development of air transportation." The Board determined that the entire profit from the route transfer constituted "other revenue" within the statutory meaning of the term, and could be used to reduce the carrier's mail pay allowance (R. 261). The Board stated, however (R. 262):

While we are required by the Act to "take into consideration" the "need" of the carrier for mail compensation together with "all other revenue," we do not understand the language of section 406 (b) as requiring us to reduce the carrier's mail pay need with any part of such "other revenue." This is a matter within our discretion. That is, we may take in "other revenue" in whole, in part, or not at all. However, we will normally use "other revenue" as available to reduce need unless there are exceptional and compelling circumstances which dictate otherwise."

The Board had first determined to reduce the mail pay allowance by the entire profits from the transaction (R. 200). On reconsideration, the Board found that there were exceptional and compelling circumstances which required that the

carrier be permitted to retain a part of the profits. In making this determination, the Board found (R. 263) that any other course of action would, in effect, override the considerations which had prompted the Board's opinion and action previously approving the sale at a profit, and would destroy the profit incentive for need carriers to effectuate route transfers necessary for the improvement of the air route pattern. The Board reduced the mail compensation by the profit derived from the sale of tangible assets, aircraft and the like, fixed at \$652,000 (R. 267-279). It declined to reduce the mail pay allowance by the profit realized from the sale of the "intangible value" of the route. Western was permitted to keep this amount, fixed at \$447,000 (R. 279), because the profit on the sale of the earning power of the route was the "factor which played the decisive part in the route transfer" (R. 264). The Board concluded (R. 265)

* * * it should again be emphasized that our decision not to include the net profit from the sale of the intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers.²

² After considering and excluding the \$447,000 profit on the sale of the intangibles, the Board determined the "break-even need" of the carrier, i. e., the amount of money necessary to equalize income and outgo, to be \$2,537,898 (R. 229, 279, 337). Return on investment at 7% was determined to

The Court of Appeals affirmed, against Western's challenge, the Board's determination that the profits from the sale of Route 68 constituted "other revenue" to Western which could be used to reduce the mail pay allowance (R. 348). The Court further held, in response to the Postmaster General's petition, that the Board mandatorily was required to reduce the carrier's mail pay by the entire profit from the sale (R. 350).

In so holding, the Court stated (R. 344) that "[t]he statute says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation." The Court recognized that "[a]llowances designed as developmental incentives for the utility whose rates are being determined are quite common in public utility rate-making" (R. 350). These developmental allowances permitted under traditional rate-making principles and by the Civil Aeronautics Act, said the Court, are restricted "to the need of each individual carrier to maintain and continue a development program of its own" (R. 349, 350). It held that the Board's determination not to offset the profit from the sale

be \$1,375,168 (R. 229, 247, 251, 279, 337). The amount necessary to satisfy actual tax liability on items recognized for mail rate purposes, \$4,295, also was provided (R. 337). Thus total mail pay for the period was allowed in the amount of \$3,917,361 (R. 339). The carrier already had received temporary mail pay of \$4,252,000, and a refund was due of \$334,639 (R. 337).

of the intangibles was for the purpose of encouraging "other carriers (not Western) to follow a given course of action" (R. 348, 349). It concluded that the statute, and a prior decision by this Court holding that the mail rate provisions describe a traditional rate-making authority,³ leave "no room for bonus subsidies not connected with the particular carrier's own need" (R. 350). Accordingly, it ordered a remand to the Board for the fixing of a new rate by deducting the entire profit from the route sale (R. 352).

SPECIFICATION OF ERRORS TO BE URGED

The Court of Appeals erred:

(1) In holding that the Board's action in permitting Western to retain the portion of the profit from the route sale which the Board previously had approved as a necessary incentive to the sale had no relation to Western's action in transferring the route or to Western's own developmental program.

(2) In holding that mail pay allowances to a given air carrier for the purpose of providing industry developmental incentive have no relation to that carrier's own developmental program.

(3) In construing Section 406 of the Civil Aeronautics Act in such manner as to restrict developmental mail pay allowances to situations in which those allowances are required for the pur-

³ *Transcontinental & Western Air, Inc. v. Civil Aeronautics Board*, 336 U. S. 601.

pose of aiding and encouraging operations and activities which are to be continued by the carrier.

(4) In holding that Section 406 of the Civil Aeronautics Act mandatorily requires the Board to reduce mail rates otherwise "fair and reasonable" by offsetting, as "other revenue" against the "need" of air carriers for mail pay, profits derived from route sales.

(5) In failing to recognize and to hold that, in fixing "fair and reasonable" mail rates, the Board has sound discretionary authority under Section 406 to refuse in appropriate cases, for reasons of regulatory policy, to offset certain categories of "other revenue" against the "need" of air carriers for mail pay allowances.

(6) In reversing the order of the Board.

REASONS FOR GRANTING THE WRIT

This case raises questions of importance in the administration of the Civil Aeronautics Act which have not been, but should be, passed upon by this Court. Although acknowledging the statutory authority of the Board to award subsidy mail pay for developmental and incentive purposes, the Court of Appeals unjustifiably has so construed the circumstances under which these allowances may be made as to seriously limit the powers conferred by Congress upon the Board to administer the mail pay provisions of the Act in such manner as to best develop a sound and

economically self-sufficient air transportation system.⁴

With the advent of larger and longer range aircraft after the cessation of hostilities in World War II, many changes in the air route pattern, designed largely for DC-3 and smaller aircraft, have become necessary for the purpose of developing sound and economically self-sufficient air carrier systems. Since most of the domestic trunkline carriers hold permanent certificates for their routes, and since the Board lacks statutory authority to compel route transfers and mergers, it must necessarily resort to persuasion and inducement to effectuate most of the desired route and carrier realignments. One such inducement is the Board's action in this case, that of permitting Western to retain the profit attributable to the sale of a route which could be operated to greater public advantage by another carrier, so that the entire industry may expect similar treatment and thus be motivated to enter into voluntary proposals for route transfers to be sub-

⁴The fact that Western happened to be conducting operations under a temporary rate at the time of the route sale is not believed to be of controlling significance to the decision below. Route sales, and sales of air carrier properties to another carrier, can be consummated only after Board approval (Sections 401 (i) and 408 of the Act, 49 U. S. C. 481 (i), 488). Both the Board and the Postmaster General are at liberty to institute new rate proceedings prior to the consummation of a particular sale so that any profits resulting therefrom may be used to reduce mail pay (Section 406 (a), *infra*, p. 17).

mitted for the approval of the Board both as to the transfer and the purchase price.

The Court of Appeals recognized the desirability of the Board's objective (R. 349), and it did not in terms deny the statutory authority of the Board to induce action such as a route transfer through permitting a carrier to retain a portion of the profit from the action. Rather, it appears to have upset the Board's order on the ground that the incentive in this case was not directed to Western, but to carriers other than Western. However, the circumstances of the case and the findings of the lower Court are such as to either effectively deny the discretionary authority of the Board to exclude certain types of "other revenue" in fixing need mail rates except where that action is for the purpose of aiding and encouraging operations and activities which are to be continued by the carrier, or to indicate that the Court erroneously applied the principles which it stated.

Western sold Route 68 because it was in need of cash to meet outstanding obligations and because from a long range standpoint operation of the route would not have been economically feasible by a regional carrier such as Western. *United-Western, Acquisition of Air Carrier Property*, 8 C. A. B. 298, 302, 303, 325. The record in the *Acquisition* case plainly discloses that the transfer of Route 68 was a step in Western's developmental program designed to enable it to con-

concentrate on regional operations, rather than continuing its dual role as both a regional carrier and one participating in transcontinental operations. See 8 C. A. B. 298, 302, 303. The Court of Appeals found that the Board, in approving the purchase price of Route 68, did so "because the profit on the transaction would provide the necessary incentive to Western to make a sale" (R. 343). Yet the Court further found that permitting Western to retain a portion of that very profit which had induced the sale had no relation to Western's action or its own developmental program (R. 348, 349). We think it obvious that permitting Western to retain the specific sum of money here involved had a sufficient relation to Western's own situation to bring it within the rule enunciated by the Court. Equally obvious, we believe, is the fact that a policy determination not to offset a particular category of "other revenue" against a carrier's mail pay need, for the purpose of encouraging similar future action by that and other carriers, has relation to the developmental program of the carrier whose action evoked the policy.

If the Court of Appeals in reality was of the view that the authority of the Board to exclude certain types of "other revenue" in fixing mail rates is limited to situations in which that action is for the purpose of aiding and encouraging operations and activities which are to be continued by the carrier, we believe the decision to be

equally erroneous and of sufficient importance to warrant review by this Court. There is nothing in the decision in *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601, or in the provisions of Section 406, which precludes the Board from excluding particular categories of other revenue in determining a carrier's mail rate for the purpose of inducing the transfer of air carrier properties and routes to carriers who can operate them to greater public advantage. We think that the statutory concept of need permits such action; the transferring carrier needs the allowance so that it will act for the "development of air transportation." (See Section 406 (b), *infra*, p. 18).

Further, the duty of the Board is to fix a "fair and reasonable" mail rate, and a rate which excludes certain categories of non-recurring capital gains does not become unreasonable as a matter of law simply because of that fact. "Need", and "other revenue" to be used in computing need, are merely factors which the Board is to "take into consideration, among other factors," in determining fair and reasonable rates. The other factors which the Board is required to take into account obviously include the developmental responsibilities placed upon the Board (See Section 2 of the Act, *infra*, p. 16). The Congress did not say that "all other revenue" must be offset against need for mail pay in all cases, or that the minimum amount necessary for continued opera-

tions always marks the limit of a fair and reasonable rate. It left to the Board the power and the duty to weigh and evaluate the various factors to be taken into account in fixing a fair and reasonable rate without binding the Board as to the part that its "consideration" of the individual factors shall play in the final determination. *cf. Secretary of Agriculture v. Central Roig Refining Co.*, 338 U. S. 604; *New York v. United States*, 331 U. S. 284, 345-349. The Court of Appeals has sharply, and we believe erroneously, limited this clear discretionary authority of the Board.⁵

⁵ Judge Prettyman, who wrote the opinion in this case, dissented from the majority opinion in the companion case of *Summerfield et al v. Civil Aeronautics Board*, U. S. App. D. C., Case No. 11,351 (not yet reported), from which petitions for certiorari also are pending before this Court. He was there willing "to agree with the Board that the elastic statutory phrase 'take into consideration' is sufficiently flexible to permit the omission of domestic earnings from the foreign calculation [of need], even after such earnings are taken into consideration."

CONCLUSION

It is respectfully submitted that this petition for certiorari should be granted.

✓ EMORY T. NUNNELEY, Jr.,

General Counsel,

Civil Aeronautics Board, Washington 25, D. C.

W JOHN H. WANNER,
Associate General Counsel,

W JAMES L. HIGHSAW, Jr.,
Chief, Litigation and Research Division,

W MORRIS CHERTKOV,

✓ O. D. OZMENT,

Attorneys,

Civil Aeronautics Board,

Washington 25, D. C.

I hereby authorize the filing of the foregoing petition for a writ of certiorari.

OSCAR H. DAVIS,

Acting Solicitor General.

APPENDIX

The pertinent provisions of the Civil Aeronautics Act of 1938, as amended,¹ are as follows:

DECLARATION OF POLICY

SEC. 2. In the exercise and performance of its powers and duties under this Act, the [Board] shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-

¹ Act of June 23, 1938, c. 601, 52 Stat. 973; Reorg. Plan No. IV, Sec. 7, effective June 30, 1940, 5 F. R. 2421, 54 Stat. 1235, 49 U. S. C. 401, et seq.

transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety, and

(f) The encouragement and development of civil aeronautics.

RATES FOR TRANSPORTATION OF MAIL

AUTHORITY TO FIX RATES

SEC. 406. (a) The [Board] is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith (including the transportation of mail by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same; and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft.

RATE-MAKING ELEMENTS

(b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board], considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 224

CIVIL AERONAUTICS BOARD, PETITIONER

v.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL
OF THE UNITED STATES; THE UNITED STATES OF
AMERICA ON BEHALF OF THE POSTMASTER GEN-
ERAL; AND WESTERN AIR LINES, INC.

No. 225

WESTERN AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMER-
FIELD, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA, ON
BEHALF OF THE POSTMASTER GENERAL

*ON WRITS OF CERTIORARI TO THE UNITED STATES
COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA
CIRCUIT*

BRIEF FOR THE CIVIL AERONAUTICS BOARD

OPINION BELOW

The opinion of the Court of Appeals for the Dis-
trict of Columbia Circuit (R. 341) is not yet re-

(1)

ported. The orders and findings of the Civil Aeronautics Board (R. 183, 258, 333) are not yet reported.

JURISDICTION

The judgment of the Court of Appeals was entered on May 4, 1953 (R. 354). The petitions for writs of certiorari were filed on July 31, 1953, and were granted on October 12, 1953 (R. 357). The jurisdiction of this Court rests on 28 U.S.C. 1254.

QUESTIONS PRESENTED

Under Section 406 of the Civil Aeronautics Act, the Civil Aeronautics Board is empowered to fix "fair and reasonable" mail rates at a level which, together with the carrier's "other revenue", will enable the carrier "to maintain and continue the development of air transportation to the extent and of the character required for the commerce of the United States, the Postal Service, and the national defense." The questions presented are:

1. Whether non-transportation revenues derived from activities incidental and related to the air carrier operations for which a mail rate is being fixed constitute "other revenue" which may be applied to reduce the rate.

2. Whether, after having approved the purchase price to be paid by an air carrier for one of the air routes of another as being in the public interest because the profit to the selling carrier would provide the incentive for the sale, the Board, in fixing a mail rate for the selling carrier, was required by Section 406 to reduce, by the amount

of profit attributable to the sale of the route, the mail pay allowance otherwise "fair and reasonable."

3. Whether the provisions of Section 406 preclude the Board from declining, as a matter of regulatory policy and for the purpose of encouraging voluntary route transfers deemed necessary in the public interest, to reduce mail rates otherwise "fair and reasonable" by the amount of profits derived from route sales.

STATUTE INVOLVED

The pertinent provisions of the Civil Aeronautics Act, which will be referred to as the Act, are set forth in the Appendix, *infra*, pp. 29 to 31.

STATEMENT

These cases arise out of a proceeding before the Civil Aeronautics Board in which a final air mail rate was fixed for a past period for Western Air Lines, Inc. Both the Postmaster General and Western were parties to the Board's proceeding, and both sought review of the Board's order. The petitions for review were consolidated for hearing and decision by the Court of Appeals (R. 355), and a single opinion and judgment were entered (R. 341, 354). The Court of Appeals affirmed the Board's order insofar as it was challenged by Western (Case No. 11324 below), and reversed the order in part upon the basis of the challenge made by the Postmaster General (Case No. 11259 below). This brief is in support of the decision

below insofar as it rejected the contentions of invalidity in the Board's order urged by Western (Case No. 225 in this Court), and also in support of the Board's contention that the Court of Appeals erred in partially reversing the order (Case No. 224 in this Court).¹

The period involved was May 1, 1944 through December 31, 1948, and operations during this period had been conducted by Western under temporary rate orders.² In 1947, during the open-rate period, Western had entered into a contract with United Air Lines for the sale, at a profit in excess

¹ These cases have been consolidated for hearing with *Civil Aeronautics Board v. Summerfield, et al.*, No. 222, and *Delta Air Lines v. Summerfield, et al.*, No. 223, which involve related issues concerning the Board's powers under the mail rate provisions of the Civil Aeronautics Act. The Board has filed a separate brief in Case No. 222.

² Prior to April, 1944, Western was conducting operations under a final service or non-subsidy rate of 60 cents per mail ton-mile for mail actually transported. In that month, the carrier petitioned the Board (R. 15) for the fixing of a need rate to be made effective from May 1, 1944, thereby in effect converting the final service rate into a temporary rate since the Board may make its new rate orders effective retroactive to the date of the institution of the rate proceeding. *Transcontinental & Western Air, Inc. v. Civil Aeronautics Board*, 336 U. S. 601. Payments continued under the 60 cent rate order until April 29, 1947, when the Board entered a new order temporarily providing a higher rate (R. 44). On December 30, 1948, the Board issued a statement of tentative findings and conclusions proposing a lump sum need payment as final mail compensation for the past period May 1, 1944-December 31, 1948, and a need rate for the future (R. 54). The proposed lump sum payment for the past period was then made effective on a temporary basis at Western's request (R. 126, 127), pending determination of the exact amount to be paid, and the proceeding to determine this precise amount was severed from the proceeding to fix the future rate (R. 135). Only the rate or lump sum payment for the past period is here involved.

of \$1,000,000, of Western's certificate and properties for air operations between Los Angeles and Denver (Route 68). After imposing appropriate conditions to insure that the portion of the purchase price paid by United in excess of the depreciated value of the physical assets would not be recouped by United from either the public or the Government, the Board approved the sale. *United-Western, Acquisition of Air Carrier Property*, 8 C.A.B. 298 (1947). As stated by the Court of Appeals (R. 343):

The Board decided that the transfer of the route at the amount to be paid by United was in the public interest, because the profit on the transaction would provide the necessary incentive for Western to make a sale and the purchasing carrier could operate the property to greater advantage to the public. The Board acted upon the premise that it has no power to force a carrier against its will to transfer property to another carrier; its only power to influence such transfers is the power of inducement. It decided that a profit on a sale would be such an inducement. Hence it approved the sale.

Section 406(b) of the Civil Aeronautics Act (*infra*, p. 31) provides in part that, in fixing "fair and reasonable" mail rates, the Board "shall take into consideration, among other factors," the "need" of the carrier for mail compensation, which, "together with all other revenue of the air carrier," will enable the carrier to "maintain and

continue the development of air transportation . . .". Western contended that the profits derived from the sale of the route and air carrier properties could not be considered by the Board in determining the mail pay allowance. It asserted that the only "other revenue" which could be taken into account was revenue derived from the sale of air transportation, or tariff revenue. The Board determined that these profits could be used to reduce the mail pay allowance (R. 261). It stated, however (R. 262):

While we are required by the Act to "take into consideration" the "need" of the carrier for mail compensation together with "all other revenue," we do not understand the language of section 406(b) as requiring us to reduce the carrier's mail pay need with any part of such "other revenue." This is a matter within our discretion. That is, we may take in "other revenue" in whole, in part, or not at all. However, we will normally use "other revenue" as available to reduce need unless there are exceptional and compelling circumstances which dictate otherwise.

The Board had first determined to reduce the mail pay allowance by the entire profits from the transaction (R. 200). On reconsideration, the Board found that there were exceptional and compelling circumstances which required that the carrier be permitted to retain a part of these profits. In making this determination, the Board found (R. 263) that any other course of action would,

in effect, override the considerations which had prompted the Board's opinion and action in previously approving the sale at a profit, and would destroy the profit incentive for need carriers to effectuate route transfers necessary for the improvement of the air route pattern. The Board reduced the mail compensation by the profit derived from the sale of tangible assets, aircraft and the like, fixed at \$652,000 (R. 264, 279). It declined to reduce the mail pay allowance by the profit realized from the sale of the "intangible value" of the route. Western was permitted to keep this amount, fixed at \$447,000 (R. 279), because the profit on the sale of the earning power of the route was the "factor which played the decisive part in the route transfer" (R. 264). The Board concluded (R. 265)

* * * it should again be emphasized that our decision not to include the net profit from the sale of the intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers.

Western also had realized some \$88,000 in profits during the period from the operation of restaurants and other concessions, including slot machines, at airport terminals used by the carrier in connection with its operations at Salt Lake City, Las Vegas and Long Beach. These revenues also were determined by the Board, again over Western's protest, to be "other revenue" available to reduce mail pay,

and the mail pay was further reduced by these incidental revenues (R. 191-195).³

The Court of Appeals (Prettyman, Proctor and Bazelon, JJ.) affirmed, against Western's challenge, the Board's determination that the revenues from the airport concessions, the profit from the sale of the intangible value of Route 68, and the profit from the sale of the tangible or operating properties accompanying the route all constituted "other revenue" to Western which could be used to reduce the mail pay allowance (R. 348, 351). The Court also held, in response to the Postmaster General's petition, that the Board was required to further reduce the carrier's mail pay by the \$447,000 profit from the sale of the intangibles (R. 350).

In holding this further reduction to be required, the Court stated (R. 344) that "[t]he statute says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation." The Court recognized that

³ After considering and excluding the \$447,000 profit on the sale of the intangibles, the Board determined the "break-even need" of the carrier, i. e., the amount of money necessary to equalize income and outgo, to be \$2,537,898 (R. 229, 279, 337). Return on investment at 7% was determined to be \$1,375,168 (R. 229, 247, 251, 279, 337). The amount necessary to satisfy actual tax liability on items recognized for mail pay purposes, \$4,295, also was provided (R. 337). Thus total mail pay for the period was allowed in the amount of \$3,917,361 (R. 339). The carrier had received temporary mail pay of \$4,252,000, and a refund was due of \$334,639 (R. 337).

The exclusion of the \$447,000 profit from the intangibles resulted in an actual return on total investment for the period involved of 9.28%. If the \$652,000 profit from the sale of the tangibles also is to be excluded, as Western contends, the carrier's return will be 12.57%.

“[a]llowances designed as developmental incentives for the utility whose rates are being determined are quite common in public utility rate-making” (R. 350). These developmental allowances permitted under traditional rate-making principles and by the Civil Aeronautics Act, said the Court, are restricted “to the need of each individual carrier to maintain and continue a development program of its own” (R. 349, 350). It held that the Board’s determination not to offset the profit from the sale of the intangibles was for the purpose of encouraging “other carriers (not Western) to follow a given course of action” (R. 348, 349). It concluded that the statute, and a prior decision by this Court holding that the mail rate provisions describe a traditional rate-making authority,⁴ leave “no room for bonus subsidies not connected with the particular carrier’s own need” (R. 350). Accordingly, it ordered a remand to the Board for the fixing of a new rate by deducting the profit from the sale of the intangible value of the route (R. 352).⁵

SPECIFICATION OF ERRORS IN NO. 224

The Court of Appeals erred:

(1) In holding that the Board’s action in permitting Western to retain the portion of the profit

⁴ *Transcontinental & Western Air, Inc. v. Civil Aeronautics Board*, 336 U. S. 601.

⁵ Judge Bazelon added a concurring opinion (R. 352) in which he expressed the view that rate-making principles are unsuited for application to subsidy mail rates, and that the statute should be amended to differentiate between compensation for the carrying of mail and payments to subsidize the development of air transportation.

from the route sale which the Board previously had approved as a necessary incentive to the sale had no relation to Western's action in transferring the route or to Western's own developmental program.

(2) In holding that mail pay allowances to a given air carrier for the purpose of providing industry developmental incentive have no relation to that carrier's own developmental program.

(3) In holding that Section 406 of the Civil Aeronautics Act mandatorily requires the Board to reduce mail rates otherwise "fair and reasonable" by deducting profits derived from route sales.

(4) In construing Section 406 of the Civil Aeronautics Act in such manner as to restrict developmental mail pay allowances to situations in which those allowances are required for the purpose of aiding and encouraging operations and activities which are to be continued by the carrier.

(5) In failing to recognize and to hold that, in fixing "fair and reasonable" mail rates, the Board has sound discretionary authority to refuse in appropriate cases, for reasons of regulatory policy, to reduce mail pay allowances by certain categories of "other revenue."

(6) In reversing the order of the Board.

SUMMARY OF ARGUMENT

I

The rate fixed for Western was a subsidy rate. The revenues derived from the route sale and the operation of restaurants and concessions at airports were considered by the Board as available

only to reduce the carrier's subsidy allowance, and not for the purpose of requiring it to transport the mail at less than a compensatory rate. These revenues grew out of and were inextricably related to Western's air carrier activities. They fell within the consistent view of the Board that the "other revenue" which may be used to reduce subsidy includes both direct transportation revenues and revenues derived from activities incidental or related to the air carrier operations for which the subsidy rate is being fixed. Congress must have intended that the Board take into account a carrier's overall position attributable to its privileged air carrier status in determining the amount of subsidy to be provided, else it would not have employed the sweeping phrase "all other revenue" in Section 406(b).

The fact that all of the other revenues here involved were not susceptible of prediction at the beginning of the rate period is inapposite. The rate was for a past period, and all items of income and expense were known. The Board was required to fix the rate in the light of available data rather than on the basis of assumed forecast. *West Ohio Gas Co. v. Public Utilities Commission of Ohio*, 294 U. S. 79.

II

Although the profit from the sale of the intangible value of Route 68 was available for the reduction of the mail pay allowance, the Board was not mandatorily required to use it for that purpose, and the Court of Appeals erred in so holding.

The Court of Appeals recognized that the Board is authorized by the statute to grant need mail pay for developmental incentive purposes, and it did not deny statutory authority to the Board to induce route transfers by permitting need carriers to retain the profits from route sales. It apparently reversed the Board's order solely because it believed that permitting Western to retain the profit from the sale of the intangibles constituted an incentive or inducement to other carriers, and had no relation to Western's action in transferring Route 68 or to Western's own developmental program. Yet the Court recognized that the Board had approved the purchase price because the profit on the intangibles was an incentive to the sale, and certainly this approval constituted a form of inducement on the part of the Board. Further, Western sold Route 68 in part because it desired to concentrate on regional operations rather than continuing its dual role as a regional carrier and as one participating in transcontinental operations. The Court erred in failing to recognize that permitting Western to retain the very profit which had motivated the transfer bore a direct relation to Western's action in selling the route and to that carrier's own developmental program.

If the Court of Appeals believed that developmental incentive allowances are permitted only for the purpose of aiding and encouraging operations which are to be continued by a carrier, we believe the decision below to be equally erroneous. In this aspect of the case, we rely upon the showing made in the Board's brief in Case No. 222

(pp. 39 to 45) that mail pay is a developmental tool to be used for the building of a sound and adequate air transportation system, and that the Board has discretionary authority to exclude particular categories of "other revenue" from the computation of mail pay allowances where that action is necessary to the development of air transportation.

ARGUMENT

Introduction

If Western is correct in its view that the only air carrier revenue which may be used to reduce mail pay allowances is transportation revenue, the question of whether the Court of Appeals erred in holding that the mail pay allowance was required to be reduced by the profit from the sale of the intangible value of Route 68 will not be reached. Accordingly, we first direct our argument to Western's contention.

- 1. The profits from the sale of Route 68 and the accompanying air carrier properties, and from the operation of the restaurants and other concessions, was "other revenue" to be considered by the Board in determining Western's mail pay allowance**

Section 406(b) of the Act (*infra*, p. 31) directs the Board in fixing mail rates to "take into consideration * * * all other revenue of the air carrier." The question of what other revenues should be taken into account arises only in the case of "need" or subsidy rates.⁶ In fixing need rates,

⁶ The Board has developed two types of mail rates under Section 406. One is the need or subsidy rate which is fixed at a level greater than that necessary to provide a fair return

the Board does not take into account all of the corporate income of a carrier. Rather, it ordinarily will reduce the rate by the amount of all transportation revenues received or anticipated from the scheduled operations, and by those other revenues which are derived "from the operation of the air carrier under its certificate of public convenience and necessity" or from an activity "related to the air carrier functions" (R. 193).⁷

on investment allocated to the mail service. The other is the service or compensatory rate, designed to provide just compensation for the service of transporting the mail. Although the statute does not distinguish between need and service rates, the Board has not considered that it should require a carrier to transport mail at less than a compensatory rate, irrespective of the extent of its "other revenue".

⁷ This interpretation of "all other revenue" by the Board accords with the well-recognized rule that "gross revenue" for public utility rate-making purposes "consists of the total income from the public utility business itself and all operations incidental to the main enterprise, but does not include income from an independent source or from property not used in the public service." 43 Am. Jur. "Public Utilities and Services", § 156. It also is consistent with a prior holding by this Court that the phrase "net earnings of the road" contained in an Act granting governmental assistance to a railroad embraces "all the earnings and income derived by the company from the railroad proper, and all the appendages and appurtenances thereof * * * and all its property and apparatus legitimately connected with its railroad", but not income unrelated to the railroad business. *Union Pacific R. R. Co. v. United States*, 99 U. S. 402, 419.

Familiar examples of incidental revenues which are considered for ordinary rate-making purposes are by-products of natural gas (*United Fuel Gas Co. v. R. R. Commission of Kentucky*, 278 U. S. 300; *Cities Service Gas Co. v. Federal Power Commission*, 155 F. 2d 694, 703 (C.A. 10); *certiorari denied* 329 U. S. 773); rentals received from concessionaires at railroad stations and other rentals from property included in the rate base (*In Re Arkansas Rate Cases*, 187 Fed. 290, 313 (E.D. Ark.), reversed on other grounds 230 U. S. 553; *Fleming v. Illinois Commerce Commission*, 388 Ill. 138, 57 N. E. 2d 384); and directory and transit advertising (*Baldwin v.*

The rate being fixed for Western was a need rate.⁸ The operation of Route 68 was an integral part of Western's air carrier business, accounting for 29% of total volume of operations (R. 69), and the sale of the route and operating properties incident thereto was possible only because of Western's operations and status as an air carrier. The operation of the restaurants and concessions also was incidental to the air carrier operations. These activities were carried on at airports for the convenience of airline passengers and employees, were financed out of air carrier working capital, utilized other assets and facilities included in Western's rate base, and were supervised by air carrier employees (R. 193-195, 266). The profits from these transactions thus fell within the Board's interpretation of "all other revenue," and accordingly were regarded by the Board as available to reduce the mail pay allowance.⁹ The Court of Appeals

Chesapeake & Potomac Tel. Co., P.U.R. 1928 E, 529 (Md. P.S.C.); *Re St. Louis-San Francisco Ry. Co.*, P.U.R. 1926 B, 669 (Mo. P.S.C.).

⁸ The service rate for Western's system in 1943 was 60 cents per mail ton-mile (*Western Air Lines, Mail Rates*, 4 C.A.B. 441), and its present service rate is 53 cents per mail ton-mile (C.A.B. Order E-6553, dated June 27, 1952). We are aware of no circumstances which would afford any basis for assuming that a proper compensatory rate for the carrier during the period here involved would have exceeded 60 cents per mail ton-mile. The allowance fixed by the Board yielded Western a return of 109 cents per ton-mile for mail actually transported. If the \$447,000 profit on intangibles excluded by the Board should be used to still further reduce the mail pay allowance, the yield would be 96 cents per ton-mile.

⁹ The greater portion of the profit from the route transfer was realized from the sale of the air carrier properties (\$652,000). Profits from the sale of operating property always have been considered as "other revenue" by the Board

affirmed the determination by the Board that the profits were to be taken into consideration in determining the mail pay allowance, but not the construction placed upon "all other revenue" by the Board. The Court stated (R. 351)

When the statute says "all other revenue" it must mean to include revenue derived from activities incidental to the operation of the airline. Whether it would also include revenue from activities unconnected with airplane operation is a question not before us and upon which we intimate no opinion.

Western's contention that the Court of Appeals erred in this construction, and that "all other revenue" means only direct transportation revenue derived from commercial rates, is wholly unpersuasive. True enough, the term "revenue" is used only twice in the Act, once in Section 406(b) and once in Section 1002(e) (49 U.S.C. 642(e)),

in fixing need rates for past periods (R. 192, 193, 264). In the only prior Board case dealing with profit from a route transfer, the profit was considered in determining the carrier's mail pay allowance. *Inland Air Lines, Mail Rates*, 1 C.A.A. 155, 162-163 (1939).

Under the Board's Uniform System of Accounts, air carriers are required to report "net revenue from incidental services" relating to items such as charter and special flights; hotel, restaurant and food services; rentals from operating properties; sales of parts, supplies and services; and the like. These incidental revenues also are customarily considered to be "other revenue" within the meaning of the Act (See R. 192, 193 and the cases there cited).

Where income is derived from an activity which is "entirely separate and apart" from the air carrier activities, it is not taken into account (R. 193). Crop dusting, private pilot training, and profits from the sale of stock of a foreign subsidiary have been regarded as falling into this latter category (See R. 193).

wherein the Board is directed to take into consideration in fixing commercial rates the "need of each air carrier for revenue." Assuming that the word "revenue" should be given the same meaning in both sections, as Western contends, it does not follow that the "revenue" mentioned in Section 1002 is restricted to tariff revenue. There is no reason why incidental revenues of a recurring nature may not be taken into account in fixing commercial rates, at least to the extent of determining whether the carrier is obtaining an overall fair return on investment. This is normal rate-making practice which must have been known and contemplated by the Congress. (See cases cited in note 7, *supra*, p. 14).

Further, if the revenue which may be considered in fixing commercial rates is only tariff revenue, it still does not follow that the word must be given the same meaning in Section 406. The meaning of the same term employed in different sections of a statute may vary according to the purposes of the sections wherein the term appears. *United States v. Champlin Refining Co.*, 341 U.S. 290.¹⁰ Section 406 permits subsidy mail pay, and Western was a subsidized carrier. The purpose of subsidy mail pay is not to afford a private benefit to air carriers, but to maintain and develop a sound and adequate air transportation system (Sections 2, 406(b), *infra*, pp. 29, 31). Certainly the Congress

¹⁰ Revenue is not defined by the Act. However, the definitions of such terms as are defined are proceeded by the admonition that such definitions are to be applicable only "unless the context otherwise requires." Sec. 1 (49 U.S.C. 401).

must have intended to permit the Board to take into account a carrier's overall position attributable to its privileged status as an air carrier in determining the amount of subsidy to be provided. It could not have meant less by the use of a term as sweeping and inclusive as "all other revenue."¹¹

Neither do the facts that rate-making ordinarily is prospective in nature, and that all of the revenues here involved were not capable of prediction at the beginning of the rate period, constitute any barrier to their consideration. All items of income and expense were known. Rates for a past period are not to be fixed upon the basis of forecast, but

¹¹ The legislative history of the Act sheds little light on the interpretation to be given to the term "all other revenue." Western placed great reliance before the Board upon the fact that the Interstate Commerce Commission had considered the phrase "revenue and profits from all other sources" as used in Section 6(e) of the Air Mail Act of 1934 (48 Stat. 936) to be restricted to only transportation revenues. However, Section 6(b) of that Act (48 Stat. 935) directed the Commission to review each year the rates of compensation there provided (not to exceed a stated amount) for the purposes of determining whether an "unreasonable profit" was being derived. The section provided that "in determining what may constitute an unreasonable profit, the said Commission shall take into consideration all forms of gross income *derived from the operation of airplanes over the route affected*" (emphasis added). Section 6(e) directed the Commission in determining "fair and reasonable" compensation to take into account "revenue and profits from all sources." The Commission, conceiving its function under the Act to be that of "fixing rates for the routes irrespective of the contractor operating them at any particular time," preferred to follow the more restrictive standard set forth in Section 6(b) which obviously conflicted with the provisions of 6(e). *Airmail Compensation*, 206 I.C.C. 675, 695-7, 720 (1935).

Further, as the Board pointed out (R. 260-261), the Air Mail Act of 1934 was not a subsidy statute, but rather was directed only to providing compensation for the carriage of the mail.

in the light of available operating data. *West Ohio Gas Co. v. Public Utilities Commission of Ohio*, 294 U. S. 79, 82. Moreover, income derived from related air carrier activities such as the operation of air ports and terminals at airports, charter and special services, rentals, and the like, can be predicted for the future with the same degree of certainty that direct transportation revenues may be predicted. Western itself predicted the amount of revenue which would be derived from these sources in submitting estimates as to its need for mail pay after January 1, 1949 (R. 93, 94). Profits from route sales and air carrier equipment cannot of course be anticipated in fixing future rates. However, route sales, and sales of air carrier properties to another carrier, can be consummated only after Board approval (Sections 401(i) and 408, 49 U.S.C. 481(i), 488). If a carrier is conducting operations under a final need rate, the Board, we believe, properly can institute new rate proceedings prior to permitting the consummation of a particular sale so that a part of the profits therefrom may be used to reduce subsidy mail pay from the date of the new rate proceeding.

Nor does the offsetting of income derived from incidental air carrier activities impose any obligation on the government to bear the risk of failure of "extra-curricular" business ventures by carriers, or result in any unfairness to the carrier, as Western contended below. Losses incurred in the operation of facilities reasonably necessary to air carrier operation, such as the operation of

airport terminals and the like, are underwritten to the extent that past or anticipated losses meet the test of "honest, economical and efficient management" (Section 406(b) *infra*, p. 31). Indeed, this test requires positive effort on the part of carriers to develop both transportation and related non-transportation revenues so that costs will be decreased (R. 195), and the taking of these revenues into account is the normal and reasonable practice of any rate-fixing agency. Further, even if a particular related air carrier activity is of such nature that losses will not be underwritten, such as the operation of slot machines, there should be no objection to the use of the profits to reduce subsidy pay unless some public purpose requires a contrary result. There is no reason for granting subsidy in a case where a carrier's revenues derived solely from its status as an air carrier are sufficient for the realization of statutory objectives.

II. The Board did not exceed its statutory authority in declining to reduce Western's mail pay allowance by the amount of profit realized from the sale of the intangible value of Route 68

Although we believe the Court of Appeals correctly held that the profit from both the sale of the air carrier properties and the intangible value of Route 68 constituted "other revenue" available for the reduction of mail pay, we think the Court erred when it held that the mail pay allowance mandatorily was required to be reduced by the profit from the sale of the intangible value of the route. Our views as to the purpose of the mail rate

provisions of the Act and the discretionary authority conferred upon the Board in administering Section 406(b) are fully set forth in the Board's brief, to which the Court's attention is respectfully invited, in *Civil Aeronautics Board v. Summerfield, et al.*, No. 222, consolidated with these cases for hearing. What has been said there will not be repeated here. We show below that the Board's action in permitting Western to retain the profit from the route sale bore a reasonable relation both to Western's own action in transferring Route 68 and to the statutory objective of developing a sound and adequate air transportation system (See Section 2, *infra*, p. 29).

The Civil Aeronautics Act was adopted in 1938 when air carriers were utilizing DC-3 or smaller aircraft. The "grandfather certificates" issued under the Act (Section 401(e), 49 U.S.C. 481(e)), and the certificates issued for some time after 1938, necessarily resulted in a route pattern designed for these small aircraft. The advent of larger, faster, and longer-range aircraft after the cessation of hostilities in World War II, together with postwar economic and transportation developments, have called for many changes in the route pattern, a fact recognized by the industry, the Board, and other agencies of government.¹² Most of the domestic trunkline carriers hold permanent certificates for their routes. There are both in-

¹² See *e.g.*, "Survival in the Air Age", A Report By The President's Air Policy Commission, 1948, p. 110; "National Aviation Policy"; Report of the Congressional Aviation Policy Board, 80th Cong., 2nd Sess., p. 26.

dividual routes and systems which would fit more logically into other systems, thereby creating new individual operating patterns which give promise of permanent economic self-sufficiency.

The Board lacks statutory authority to compel route transfers and mergers.¹³ It has not believed that it should withhold mail pay from a carrier operating a route required by the public convenience and necessity for the purpose of forcing a transfer or merger. See *United-Western, Acquisition of Air Carrier Property*, 8 C.A.B. 298, 323 (1947). Accordingly, it has employed various methods of persuasion and inducement to encourage voluntary adjustments in the route pattern. These methods have included the suggesting of various mergers and consolidations deemed appropriate by the Board, and the permitting of route transfers at a profit to the selling carrier.

The determination to permit route transfers at a profit represented a major policy determination by the Board and was announced in connection with the transfer of Route 68. *United-Western, Acquisition of Air Carrier Property*, 8 C.A.B. 298 (1947). Western was a regional carrier operating in the Western section of the United States, and the Los Angeles-Denver route was of primary im-

¹³ Section 401(h) of the Act (49 U.S.C. 481 (h)), authorizes the Board to "alter, amend, modify, or suspend" certificates. The Board as presently advised considers that it is authorized by this section to suspend or withdraw one carrier's certificate authority and to substitute service by another carrier only where such action will not result in a transformation of the essential character of the first carrier's operation. *Western Air Lines v. Civil Aeronautics Board*, 196 F. 2d 933 (C.A. 9), cert. den. 344 U. S. 875; *United Air Lines v. Civil Aeronautics Board*, 198 F. 2d 100 (C.A. 7).

portance as a link to transcontinental operations. Western desired to concentrate on developing regional operations, and the operation of Route 68 would not have been economically feasible on the part of a regional carrier from a long-range standpoint. Moreover, Western was in need of cash to meet outstanding obligations. See 8 C.A.B. 298, 302, 303, 325. The route fitted more logically into United's system. The Board, with one member dissenting, was of the view that allowing Western to make a commercial profit on the sale would be in the public interest since this and other route transfers otherwise would, except in rare instances, be unlikely. 8 C.A.B. 298, 323, 341. Accordingly, it determined to permit route transfers at a profit in appropriate cases irrespective of whether the transferring carrier was a subsidy or service rate carrier.

It first concluded in this case that other incentives would provide a sufficient spur for such transfers in the case of subsidized carriers (R. 198, 199). One member dissented, characterizing the Board's action as a "penny-wise and pound-foolish" decision (R. 231). On reconsideration, the Board reverted to its original views as expressed at the time of the transfer. It pointed to the fact that the profit to Western on the sale of the earning power or intangible value of Route 68 was the "factor which played the decisive part in the route transfer" (R. 264). It stated (R. 263):

It was the Board's serious concern in the *Acquisition* case that unless Western were allowed a "commercial profit" from the then

proposed transaction, the Board would be thwarting the improvement of the air pattern through voluntary action by the carriers. Improvement of the national air pattern has been for some time, and still is, a primary objective of the Board. It should be apparent, therefore, that we must consider the possible effect of our action in this proceeding on what the Board was trying to accomplish in the *Acquisition* case. If we now decided to deny Western the right to keep any part of the profit permitted in that case, we would, in effect, override the considerations which prompted the opinion and destroy the possibility of the incentive which the Board found so important. In order to avoid the danger of confining the present air pattern to a rigid mold, and to continue to encourage voluntary action by the carriers, we believe that the incentive of profit which may be derived from the sale of a route so clearly approved in the *Acquisition* case should be preserved here.

Accordingly, the Board determined not to reduce Western's mail pay by the profit from the sale of the intangible value of the route since it concluded that a denial to Western of some commercial profit on the sale would constitute a thwarting of improvement in the air transportation pattern through voluntary action by the carriers, and because the Board was seeking in this manner to spur the development of a self-sufficient air transportation industry (R. 263-265).

The Court of Appeals reversed the Board's order

solely on the ground that the Board had exceeded its statutory authority, and not because the Court believed the action to be unreasonable or unrelated to permissible statutory objectives. Indeed, the Court of Appeals recognized the "force of the Board's description of the desirability of encouraging carriers to transfer routes and other property" (R. 349), thereby rejecting, we believe, the Postmaster General's contentions below that the Board's action was unreasonable.¹⁴ The Court of Appeals also rejected, in this case, the Postmaster General's contention that need mail pay may be awarded only in that minimum amount necessary to sustain an existing or projected operation and to provide a stated rate of fair return on investment. The Court expressly recognized (R. 344) that Section 406 "says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation," and that "allowances designed as developmental in-

¹⁴ The Postmaster General had urged below that the Board's action, if within statutory authority, was unnecessary and unreasonable in that other sufficient means existed for effectuating desired changes in the route structure, and that no reasonable basis existed for a belief that other voluntary transfers would result from the Board's action in this case. These arguments, which go to the wisdom of the Board's action, centered around the statements in the tentative opinion wherein the Board had first determined to offset the entire profit from the route transfer (R. 195-200). The Board's ultimate conclusion was within the realm of rational inference, and related to a matter within its competence. The fact that the ultimate conclusion reached after fuller consideration was different from the one first stated is of no legal significance. See *e.g.*, *Shein v. United States*, 102 F. Supp. 320 (D. N.J.), affirmed per curiam 343 U.S. 944.

centives" are permissible (R. 350). It did not in terms deny the statutory authority of the Board to induce action such as a route transfer through permitting a carrier to retain a portion of the profit from the transfer. Rather, it appears to have upset the Board's order solely on the ground that permitting Western to retain the profit from the sale of the intangibles was for the purpose of encouraging "other carriers (not Western) to follow a given course of action" (R. 348, 349), and because the action had no relation to Western's own "development program" (R. 350).

We think it obvious that the Board's action in permitting Western to retain the sum of money here involved had a sufficient relation to Western's own situation to bring it within the rule enunciated by the Court. The sale was a step in Western's "development program" for concentrating on regional operations (*supra*, p. 23). Western had responded to the profit incentive, and the Court found that the Board approved the purchase price of Route 68 "because the profit on the transaction would provide the necessary incentive to Western to make a sale" (R. 343). Presumably, under the Court's reasoning, the Board could announce that, for the purpose of encouraging route transfers, the profit derived from the sale of the intangible value of the route would not be used to reduce mail pay, and then adhere to that position with respect to any "need" carrier which sold a route in reliance upon the representation. However, routes may be transferred only by leave of the Board and at a

price which the Board approves as being in the public interest (Section 401(i), 49 U.S.C. 481(i)). The Board of course did not promise Western in the *Acquisition* case that it could retain the profit from the sale of the intangibles. Nonetheless, when the Board approves a certificate sale at a profit for the purpose of encouraging route transfers, as in the case of Route 68 (8 C.A.B. at p. 323), we think the carrier could reasonably expect to be permitted to retain the profit attributable to the sale of the certificate, and that the approval of the purchase price represents an inducement for the transfer on the part of the Board. Further, administrative policy may be formulated on a case-to-case basis rather than by general rule. We believe that a policy determination not to reduce need mail pay by particular categories of "other revenue" has the same relation to the developmental program of the carrier whose action evoked the policy that it has to those of the carriers who come after.

If we have misconceived the basis for the reversal of the Board's order, and if the Court of Appeals in reality was of the view that developmental allowances are permitted only for the purpose of aiding and encouraging activities which are to be continued by the carrier, we believe the decision below to be equally erroneous. In this aspect of the case, we rely upon the showing made in the Board's brief in Case No. 222 (pp. 30 to 45) that mail pay is a developmental tool to be used for the building of a sound and adequate air transportation system,

and that the Board has discretionary authority to exclude particular categories of "other revenue" from the computation of mail pay allowances where that action is necessary to the development of air transportation. We also note here, as there, that, after full consideration, the Board found the rate fixed for Western to be "fair and reasonable" (R. 338). The statute required no more.

CONCLUSION

The judgment below should be reversed only insofar as it set aside the order of the Board.

Respectfully submitted,

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APPENDIX

The pertinent provisions of the Civil Aeronautics Act of 1938, as amended,¹⁵ are as follows:

DECLARATION OF POLICY

SEC. 2. In the exercise and performance of its powers and duties under this Act, the [Board] shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-trans-

¹⁵ Act of June 23, 1938, c. 601, 52 Stat. 973; Reorg. Plan No. IV, Sec. 7, effective June 30, 1940, 5 F. R. 2421, 54 Stat. 1235, 49 U. S. C. 401, et seq.

portation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety, and

(f) The encouragement and development of civil aeronautics.

RATES FOR TRANSPORTATION OF MAIL

AUTHORITY TO FIX RATES

SEC. 406. (a) The [Board] is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith (including the transportation of mail by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same; and

the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft.

RATE-MAKING ELEMENTS

(b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board], considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case the [Board] shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 224

CIVIL AERONAUTICS BOARD, PETITIONER

v.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL OF
THE UNITED STATES; THE UNITED STATES OF
AMERICA ON BEHALF OF THE POSTMASTER GEN-
ERAL; AND WESTERN AIR LINES, INC.

No. 225

WESTERN AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMER-
FIELD, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA, ON
BEHALF OF THE POSTMASTER GENERAL

*ON PETITIONS FOR WRITS OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE DIS-
TRICT OF COLUMBIA CIRCUIT*

**MEMORANDUM FOR THE POSTMASTER GENERAL AND
THE UNITED STATES OF AMERICA**

The principal issue raised in these petitions is
whether Section 406 (b) of the Civil Aeronautics

(1)

Act of 1938, 52 Stat. 998, 49 U.S.C. 486, requires the Civil Aeronautics Board, in fixing an air carrier's subsidy mail pay, to offset *all* of the carrier's other revenue, or whether, as the Board held, it may in its discretion refuse to offset some portion of such revenue.¹ The Board, in fixing petitioner Western Air Lines' subsidy for the period 1944 to 1948, refused to offset a \$447,000 profit made by the carrier on the sale of one of its routes in 1947. The Board did so on the ground that Western should be permitted to "retain" this profit in order to encourage voluntary route transfers by other carriers (R. 263-264). The court of appeals unanimously reversed the Board on that issue. The court held that Section 406 (b) restricts subsidy payments "to the need of each individual carrier," and does not authorize the Board to use subsidy payments "to provide incentives [for route transfers] to the industry generally" (R. 349-350).

We believe that the court of appeals correctly held that the Board erred in failing to offset the \$447,000 profit in fixing the carrier's subsidy need.²

¹ Section 406(b) directs the Board, in determining a carrier's subsidy need, to "take into consideration * * * the need of each such air carrier for compensation * * * sufficient * * * *together with all other revenue of the air carrier*, to enable such air carrier * * * to maintain and continue the development * * *" of a national air transportation system [emphasis added].

Petitioner in No. 225 raises the further question (Pet. 12) whether the "other revenue" referred to in this Section is limited to revenue derived from the transportation of persons and property, or whether, as the Board held, it embraces the broader category of all income derived from air carrier functions.

² We note that petitioners erroneously state the issue when they refer to Western's "retaining" the profit on the sale (*e.g.*,

However, since we recognize that the basic statutory question involved—whether the Board can refuse to offset portions of a carrier's other revenue in determining subsidy—is of public importance, we do not oppose the petitions.³ If the petitions are granted we intend to support the decision below not only for the reasons stated by the court, but on the broader ground that under the Act the Board cannot award subsidy in excess of a carrier's need, and that in determining such need the Board is required to offset *all*—and not just a part—of the carrier's other revenue.

Respectfully submitted,

ROBERT L. STERN,
Acting Solicitor General.

AUGUST, 1953.

Pet. No. 224, 10, 12; Pet. No. 225, 11, 13). Clearly, no portion of the profit is "taken away" when subsidy is awarded; the only issue is how much *additional* money the carrier is to receive from the public treasury.

³ We wish to point out, however, that pursuant to Reorganization Plan No. 10 of 1953, 18 Fed. Reg. 4543, subsidy payments for services rendered after October 1, 1953, will be made by the Board, and not by the Postmaster General. Thereafter, the Postmaster General will make only payments covering compensation for the carriage of mail.

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In the Supreme Court of the United States

OCTOBER TERM, 1953

No. 224

CIVIL AERONAUTICS BOARD, PETITIONER

v.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL
OF THE UNITED STATES, THE UNITED STATES OF
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No. 225

WESTERN AIR LINES, INC., PETITIONER

v.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMER-
FIELD, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA,
ON BEHALF OF THE POSTMASTER GENERAL

*ON WRITS OF CERTIORARI TO THE UNITED STATES COURT
OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT*

**BRIEF FOR THE POSTMASTER GENERAL AND THE UNITED
STATES OF AMERICA**

OPINIONS BELOW

The opinion of the United States Court of Appeals
for the District of Columbia Circuit (R. 341-353) is
reported in 207 F. 2d 200. The opinions of the Civil

(1)

Aeronautics Board (R. 54-125, 183-253, 258-281, 333-339) have not yet been published.

JURISDICTION

The judgment of the Court of Appeals was entered on May 4, 1953 (R. 354). The petitions for writs of certiorari were filed on July 31, 1953, and were granted on October 12, 1953. The jurisdiction of this Court is conferred by 28 U. S. C. 1254 (1).

QUESTIONS PRESENTED

In fixing subsidy mail pay for a past period, the Civil Aeronautics Board refused to offset the portion (\$447,000) of the total profit (\$1,099,000) made by a carrier on the 1947 sale of one of its routes and related equipment which represented the value of the transferred certificate of public convenience and necessity. Section 406 (b) of the Civil Aeronautics Act directs the Board, in fixing mail pay subsidy, to "take into consideration * * * the need of each such air carrier for compensation * * * sufficient * * * together with all other revenue of the air carrier, to enable such air carrier * * * to maintain and continue the development * * *" of a national air transportation system. The questions presented are:¹

¹ We do not discuss the other questions raised by petitioner Western in No. 225 that the Board awarded it insufficient subsidy by erroneously offsetting certain other portions of its revenue. These issues, which the Court of Appeals decided against Western, are discussed in petitioner Board's brief, pp. 13-20. We support the position there taken that those other items of revenue properly were used to reduce the carrier's mail pay need.

1. Whether Section 406 (b) of the Act empowers the Board to award a subsidy in the form of "need" mail pay which exceeds the carrier's actual "need."

2. Whether Section 406 (b) requires the Board, in determining a carrier's "need" for subsidy, to offset "all other revenue of the air carrier," or whether the Board may, in its discretion, offset only a part of such other revenue.

3. Whether the carrier "needed" the additional \$447,000 subsidy which it received as a result of the Board's refusal to offset the profit on the sale of the certificate.

STATUTE INVOLVED

The Civil Aeronautics Act of 1938, 52 Stat. 973, as amended, 49 U. S. C. 401, *et seq.*, provides in pertinent part as follows:

Section 401 (h) The [Board], upon petition or complaint or upon its own initiative, after notice and hearing, may alter, amend, modify, or suspend any such certificate, in whole or in part, if the public convenience and necessity so require, or may revoke any such certificate, in whole or in part, for intentional failure to comply with any provision of this title or any order, rule, or regulation issued hereunder or any term, condition, or limitation of such certificate:
* * * [49 U. S. C. 481 (h).]

* * * * *

Section 401 (j) No certificate shall confer any proprietary, property, or exclusive right in the use of any air space, civil airway, land-

ing area, or air-navigation facility. [49 U. S. C. 481 (j).]

* * * * *

Section 406 (a) The [Board] is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, * * * and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft. [49 U. S. C. 486 (a).]

Section 406 (b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board], considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of

mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense. [49 U. S. C. 486 (b).]

STATEMENT

Petitioners challenge the correctness of the Court of Appeals' decision that the Civil Aeronautics Board awarded excessive mail pay subsidy to petitioner Western Air Lines ("Western"). The court held that, in determining Western's subsidy need, the Board had departed from the applicable statutory standard in failing to offset part of the profit made by Western on the sale of one of its routes to United Air Lines ("United"). A brief description of the certification and route transfer proceedings is necessary for an understanding of the case.

THE CERTIFICATION AND ROUTE TRANSFER PROCEEDINGS

On November 11, 1944, the Board issued a certificate of public convenience and necessity to Western for a new route (route 68) between Denver, Colorado, and Los Angeles, California. *Western Air Lines, Denver-Los Angeles Service*, 6 C. A. B. 199, affirmed *sub nom. United Air Lines v. Civil Aeronautics Board*, 155 F. 2d 169 (C. A. D. C.). The Board selected

Western over United, the principal other applicant, because award of the route to United "would divert so much traffic from Western as to seriously impair that carrier's ability to continue as a strong independent air carrier in a position to compete for traffic in the western section of the country," and would make Western "dependent upon the Government for substantial subsidies in the form of mail compensation in order to provide the service contemplated in its existing certificates." 6 C. A. B. 210. The Board concluded that maintenance of Western "as a strong regional carrier in a position to compete effectively" in its service area "outweighs any benefits which might accrue from the establishment of [the] additional single-company service from Los Angeles to the east via Denver" which United could provide. *Id.* at 212.

Western did not inaugurate service over route 68 until April 1, 1946 (R. 59). Less than a year later Western and United entered into an agreement, subject to approval by the Board, for the sale of the certificate and route, together with aircraft and equipment used thereon, to United for \$3,750,000. The purchase price represented a substantial profit to Western over the cost of the tangible property to be transferred.²

On August 25, 1947, the Board approved the sale as "consistent with the public interest." *United*

² Route 68 was the only one on which Western made a profit during 1946. During the nine months of that year when the route was in operation, it earned approximately \$640,000. 8 C. A. B. 298, 301.

Air Lines-Western Air Lines, Acquisition of Air Carrier Property, 8 C. A. B. 298, 324. The Board pointed out that Western's president had testified that in his view Western's "dual role" as a regional and a transcontinental carrier was "one of the primary causes" of the carrier's financial difficulties;³ that Western should withdraw from the transcontinental field and "concentrate on a regional service";⁴ and that United's routes made it the logical carrier to take over route 68 (*id.* at 303). The Board noted that the purchase price exceeded Western's depreciated original cost of the tangible property transferred by \$2,000,000, of which \$1,500,000 represented the value of the route. *Id.* at 312.⁵ It found, however, that sale of the route at a profit would not be "adverse to the public interest" (*id.* at 324), since prohibition of certificate transfers "at a commercial profit" would eliminate the carriers' "incentive" to transfer routes to other carriers "who would be in a

³ Western had "major obligations" of several million dollars coming due in February, 1947, which, if not extended or met, "could have resulted in receivership or bankruptcy". Market conditions in January, 1947, precluded the carrying out of a previously planned financing program for the company. Western's balance sheet as of February 28, 1947, showed current assets of approximately \$3,800,000 and current liabilities in excess of \$10,000,000, 8 C. A. B. 302.

⁴ He stated that effective development of Route 68 would have required Western to undertake full transcontinental operations at an estimated capital outlay of \$85,000,000. 8 C. A. B. at 302.

⁵ The Board found that the \$3,750,000 purchase price was a fair one reached through arms-length bargaining. 8 C. A. B. at 314-315.

position to operate them with greater advantage to the public interest," and would "'freeze' the air pattern of the Nation to its present design * * *" (*id.* at 323). But, in order to prevent "inflation of the investment rate base" and "potentially higher charges to the public," the Board required United to make an immediate charge to surplus of the \$2,000,000 item of intangibles (*id.* at 318-319).

Chairman Landis, dissenting, disapproved the transaction unless the purchase price were reduced by the \$1,500,000 representing the value of the route. He stated that the parties should not be permitted to "traffic in air certificates," since Congress had stated that there is "no private proprietary right in air transportation that can be made the subject of barter and sale—the subject of an additional claim against the public" (*id.* at 344). He added that Western "actually" would be "giving up very little" in relinquishing the \$1,500,000, since under "any theory" that sum is "profit to Western and as such is revenue under section 406 (b) of the Civil Aeronautics Act which the Board must take into consideration in fixing any need rate." "The Board," he concluded, "thus must in the last analysis charge the subsidy that Western will get and upon which it must depend with that amount, so that in the end Western's acquisition of \$1,500,000 becomes only a temporary advance against future subsidy payments" (*Id.* at 344-345).

THE MAIL PAY PROCEEDINGS

On April 26, 1944, Western petitioned the Board to increase its mail pay (R. 15).⁶ A temporary higher rate was fixed by the Board in April 1947 (R. 44-48). On December 31, 1948, the Board issued Tentative Findings and Conclusions (R. 54) proposing total subsidy mail pay of \$4,252,000 for the period May 1, 1944, to December 31, 1948, together with an order to show cause why the proposed mail pay award should not be made final (R. 124-125).⁷ In calculating this subsidy, the Board treated the entire profit from the sale of route 68 as "other revenue of the air carrier" which, under Section 406 (b) of the Act, would "serve to reduce Western's 'need' for mail compensation" (R. 68), and accordingly offset the total profit in ascertaining the carrier's need.

1. *The Board's First Decision.*—After full administrative proceedings,⁸ the Board issued its first decision (R. 183-253). The Board again held that Western's entire net profit on the sale—which it calculated at \$1,099,000 (R. 196)⁹—constituted

⁶ Western was then on a so-called service or compensatory rate, which the Board had fixed in November 1943. *Western Air Lines, Mail Rates*, 4 C. A. B. 441.

⁷ The Board also proposed a prospective mail pay rate to become effective January 1, 1949 (R. 91-104). This rate became final on May 6, 1949. *Western Air Lines, Mail Rates*, 10 C. A. B. 285.

⁸ Exceptions were filed to the tentative findings (R. 127), hearings were held, briefs were filed, and the Board heard oral argument (R. 185).

⁹ Western's book profit of \$2,124,000 was reduced by a number of offsets against such profit (R. 70, 82, 196-197, 212-220, 264).

"other revenue" which should be offset in determining Western's need for mail pay subsidy. The Board stated that it was "clear that to the extent that there was a profit [on the sale], Western's need for mail pay support was reduced accordingly" (R. 195). Pointing out that the profit arose from the sale of "air carrier property," the Board refused to differentiate between the tangible and the intangible elements of the sale. It stated that these elements "go together to make up one transaction"; that the profit from the intangibles was no "less valid" a source of other revenue than that from the tangibles, since both were received "by virtue of benefits accruing to Western from its certificate of public convenience and necessity, which it received from the Government"; that it would be "contrary to the public interest" to use public funds to "subsidize a need which had already been covered by profits accruing from benefits under the certificate"; and that offsetting the profit on the sale of the intangibles "in no sense" curtailed the carrier's rights under its certificate, which include the right to subsidy mail pay "based upon need," but merely offset against these rights "all special benefits in the form of profits realized by virtue of having been awarded the certificate" (R. 197-198).

The Board specifically rejected Western's contention that inclusion of the total profit as "other revenue" would "adversely affect the incentive for air carriers to accomplish necessary route adjust-

ments through voluntary route transfers and mergers or consolidations" (R. 198). The Board pointed out that

The incentive of a carrier wishing to dispose of a route or to merge is to correct a situation which is inimical to its best interests, such as the operation of an uneconomical route that will mitigate against its over [ever] reaching self-sufficiency. The incentive to divest itself of such a route should be reinforced by the realization that *subsidy mail pay will not be forthcoming to perpetuate an uneconomic route pattern* [*ibid.*, emphasis added].

The Board further noted that the record did not indicate that Western would not have sold the route had it known that the profit would be treated as "other revenue" for subsidy purposes (R. 198-199); that Western had "no basis for believing otherwise" (R. 199); and that the fact that the "outstanding example" of an airline merger since the sale—the purchase of American Overseas Airlines, Inc. by Pan American Airways, Inc.—had been consummated at book value indicated that the "profit motive" is not such a "necessary consideration for the accomplishment of route transfers or mergers as Western would have us believe" (*ibid.*)¹⁰.

The Board accordingly offset Western's entire profit of \$1,099,000 in calculating that the carrier's

¹⁰ The Board pointed out that in approving the sale of route 68 it had not been "concerned with the issue of the treatment of any profit realized by Western in relation to its need for mail pay" (R. 196; see R. 262).

break-even need was \$2,087,000 (R. 229).¹¹ To this the Board added \$134,686 representing the carrier's estimated tax liability, and \$1,358,840 representing a 7% return for each of the years involved on the carrier's adjusted investment base ¹² (*ibid.*). Total subsidy mail pay was thus fixed at \$3,580,526, or \$671,474 less than the \$4,252,000 temporary mail pay that Western already had received (*ibid.*).

2. *The Board's Second Decision.*—Exceptions to the Board's decision were filed by the Postmaster General and by the carrier (R. 254-257), and the Board heard oral argument (R. 258).¹³ The Board's decision on the exceptions (R. 258-281) reversed its prior holding, and refused to offset the \$447,000 profit (R. 264) on the sale of the route in fixing Western's subsidy.¹⁴

¹¹ The Board also offset other non-flight revenue, including restaurant and concession income (R. 191-195). And, in determining Western's break-even point, the Board disallowed certain expenses which did not meet the statutory standard of "honest, economical, and efficient management." Thus, excessive maintenance costs were reduced (R. 207), excess general and administrative expenses were scaled down (R. 212), and depreciation on unneeded aircraft was disallowed (R. 223).

¹² In determining Western's investment base, the Board excluded certain items—such as excess aircraft—which did not reflect "economical and efficient management" (R. 247).

¹³ The Air Transport Association of America, a trade association of air carriers, filed a brief *amicus curiae* supporting, *inter alia*, Western's contention that the profit from the sale of the route was not "other revenue" (R. 258-259).

¹⁴ In its second decision the Board for the first time referred to its prior decision as a "tentative" one (R. 258). In its first decision the Board had stated that the matter was then before it "for our decision" (R. 185).

The Board reaffirmed its prior holding that the entire profit on the transaction—tangibles as well as intangibles—constituted “other revenue” within Section 406 (b) (R. 261).¹⁵ However, the Board distinguished between the two elements, and held that it was “appropriate” to allow Western to “keep the net profit from the sale of the intangibles” (R. 264).

The Board reasoned that the statutory requirement that it “take into consideration” the “need” of the carrier, together with all its other revenue, did not require it to reduce the carrier’s mail pay “need” with any part of such other revenue; that this was a matter for its discretion; and that it might “take in” such other revenue “in whole, in part, or not at all” (R. 262). The Board stated that it had approved the sale of route 68 at a profit “because it would provide the necessary incentive for Western to dispose of the properties to another carrier which was in a position to operate them with greater advantage”; that it was the Board’s “serious concern” in so doing that unless Western were allowed a “commercial profit,” the Board would be “thwarting the improvement of the air pattern through voluntary action by the carriers” (R. 262–263); that if the Board were to

¹⁵ The Board stated that it could see “no distinction * * * between the net revenues derived from the sale of tangibles such as operating property and equipment, and the net revenues received from the intangible elements of the sale such as the earning power of the route. Both kinds of revenue originated in the same transaction and augmented the carrier’s net income. Both must be considered in relation to the carrier’s ‘need’ ” (R. 261).

"safeguard the incentive for voluntary route transfers," it could not refuse Western the right "to retain at least some portion" of the profit (R. 264); and that, although the tangible and intangible elements together "made up the single transaction," they could be separated to determine "whether, and to what extent," the other revenue should be offset against Western's "need" (*ibid.*).

The effect of the Board's ruling on this issue was to increase Western's subsidy by \$447,000 over the amount allowed in the first decision.¹⁶

THE DECISION OF THE COURT OF APPEALS

On the Postmaster General's petition to review, the Court of Appeals unanimously held that the Board had erred in failing to offset the \$447,000 profit on the sale of the route.¹⁷ The court pointed out that the Board had not found that "Western itself" needed the additional \$447,000 subsidy, but only that the additional amount was given "in order to encourage

¹⁶ The Board, after making further adjustments in the carrier's expenditures and tax allowance (R. 333-337), awarded Western total subsidy mail pay of \$3,917,361 (R. 337). Since Western previously had received temporary mail pay of \$4,252,000, the carrier was found to have received an overpayment of \$334,639 (*ibid.*).

The Postmaster General's petition for reconsideration, which challenged the refusal to offset the \$447,000, was denied by the Board without discussion of the issue (R. 333, 337).

¹⁷ The carrier filed a separate petition to review, alleging that the Board had awarded it insufficient subsidy. The court rejected the carrier's contentions (R. 345-348, 350-351) See *supra*, p. 2, n. 1.

other carriers (not Western) to follow a given course of action" (R. 348-349). The court held that the Act does not authorize the Board "to provide incentives to the industry generally" for the development of air transportation, but restricts subsidy payments "to the need of each individual carrier to maintain and continue a development program of its own" (R. 349-350).

The court stated that it was erroneous to speak of "offset[ing]," "deduct[ing]," or "recaptur[ing]" profit by including it in revenue, since the need contemplated by the Act was a "net figure" which appears "necessary over and above that which the carrier has," and not a gross figure from which offsets or reductions were made (R. 351). The court added that (R. 351-352):

* * * the passenger revenue, etc., is not "offset" against or "deducted" from the need of the carrier. None of the earned revenue is recaptured. The bare, uncomplicated situation is that when the carrier has substantial revenues from non-mail sources the margin of its need for mail pay is less.

SUMMARY OF ARGUMENT

Our statutory arguments under Points I and II are fully set forth in our brief in Nos. 222 and 223, this Term, and are merely summarized here.

I. Mail pay is fixed by the Civil Aeronautics Board either on a "service" rate, which constitutes fair compensation for carrying the mail, or on a "need" rate, which is an outright subsidy to enable

the carrier to earn a stated return on its investment. Section 406 (b) of the Act imposes a clear duty on the Board to limit subsidy to such amount as will meet the carrier's need as therein defined. In the instant case, the carrier received subsidy designed to give it an ample 7 percent return after taxes.

II. The Board declined to offset Western's profit on the sale of the route—admittedly “other revenue” of the carrier—on the theory that the Act gives it “discretion” to “take in ‘other revenue’ in whole, in part, or not at all.” The Act, however, requires the Board to offset *all* of the carrier's other revenue, and the Board has no discretion to offset only some of it. Western's profit from the sale of the route reduced its need for subsidy from the public treasury just as much as the profits from the sale of equipment used on that route, or from restaurant and slot machine concessions. By failing to offset the profit on the certificate, the Board gave Western \$447,000 more subsidy than it needed.

III. There is no issue here as to Western's right to “retain” any portion of the profits on the sale of the route. Western retains every penny of that profit. The only issue is how much additional money Western is to receive as a subsidy from the public treasury.

The extra subsidy was not needed to induce Western itself to sell the route. Indeed, the Board's decision makes it clear that Western was given the additional subsidy in order to encourage other carriers to effect route transfers. The Act, however,

makes the need of the individual air carrier the basis for subsidy, and does not authorize the Board to award subsidy to provide incentives to the industry generally.

There is no basis for the Board's only justification for its refusal to offset, that other carriers would refrain from making route adjustments if profits on such transfers were not to be duplicated with subsidy. The Board has adequate authority to encourage route transfers through its other powers under the Act. Retention of a route not economically adapted to the carrier's operations constitutes a failure of "economical and efficient management" which should result in reduction of subsidy. Needed changes in the route pattern can also be effected by the Board through its power under Section 401 (h) of the Act to "alter, amend, modify, or suspend" any certificate, in whole or in part. Moreover, mergers and consolidations can accomplish route alterations.

ARGUMENT

INTRODUCTION

In setting aside the Board's order, the Court of Appeals held that the Board had erred in awarding Western an additional \$447,000 subsidy "in order to encourage other carriers (not Western) to follow a given course of action" (R. 348-349). The Court stated that the Act does not authorize the Board "to provide incentives to the industry generally" for the development of air transportation, but restricts subsidy payments "to the need of each individual

carrier to maintain and continue a development program of its own" (R. 349-350). While we believe that the court was correct in this conclusion, we do not rely solely on this basis to support the decision below, but also rest on the broader ground that under the Act the Board cannot award subsidy in excess of a carrier's need, and that in determining such need the Board is required to offset *all*—and not just a part—of the carrier's other revenue. Thus, even if the Board were correct in its contention (Br. 26-27) that the incentive in this case was for Western itself, and not for the industry generally—which we dispute (see *infra*, pp. 23-26)—that fact would not validate its refusal to offset the \$447,000.

These same general statutory questions as to the Board's duty to offset all other revenue also are involved in Nos. 222 and 223, which have been consolidated with the instant case for argument. We have fully set forth our arguments on those issues in our brief in that case, and will not repeat them at length here. In sections I and II of this brief we will merely summarize our position, and refer the Court to the portions of our brief in Nos. 222 and 223 which discuss those issues in detail.

I.

SUBSIDIES IN THE FORM OF MAIL PAY CANNOT EXCEED THE "NEED" OF THE CARRIER

Section 406 (b) of the Civil Aeronautics Act requires the Board, in fixing "fair and reasonable" rates of compensation for the transportation of mail by aircraft, to "take into consideration," *inter alia*,

* * * the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

In fixing mail pay, the Board has recognized the distinction which the Act thus makes between compensation sufficient (1) to insure the transportation of mail, and (2) to enable the carrier "to maintain and continue the development" of a national air transportation system. Mail pay for economically self-sufficient carriers is fixed on a so-called "service rate." This constitutes fair compensation for carrying the mail, is based on mail miles flown, actual or prospective, and supposedly contains no element of subsidy. If, on the other hand, the carrier is not operating profitably, then it is given what the Board calls a "need rate." This bears no relation to carriage of mail at all, but is an outright subsidy designed to enable the carrier to meet its expenses, pay its taxes, and earn a stated return on its recognized investment base. (Brief, Nos. 222 and 223, pp. 17-18.) Western received "need" mail pay in the instant case designed to give it the 7 percent return after taxes which the Board customarily allows for past periods (R. 226).

Section 406 (b) imposes a clear duty on the Board to limit subsidy to such amount as will meet the carrier's "need" as defined in that section. Although "need" is not the only factor which the Act requires the Board to consider, it plainly is a limiting one, *i. e.*, the Board cannot award subsidy in excess of what the carrier actually needs. Congress could hardly have intended, after providing the "carefully worded 'need' formula which the Act sets for the Board's guidance in fixing the air mail 'compensation'," *American Airlines, Mail Rates*, 3 C. A. B. 323, 335, to permit the Board to disregard this standard by determining and "considering" such need, and then awarding a subsidy in excess thereof. Plainly, the Act sets the carrier's "need" as the ceiling on subsidy mail payments. See Brief, Nos. 222 and 223, pp. 16-22.

II.

SECTION 406 (B) REQUIRES THE BOARD, IN DETERMINING A CARRIER'S SUBSIDY NEED, TO OFFSET ALL—NOT JUST SOME—OTHER REVENUE OF THE CARRIER

In fixing Western's mail pay subsidy, the Board in its initial decision first determined the carrier's break-even need by calculating the difference between the carrier's nonmail revenues and total allowable expenses.¹⁸ These nonmail revenues included restaurant and concession income (R. 191-195) and the entire profit on the sale of route 68 (R. 195-200), as well as flight income. In holding that the restaurant

¹⁸ The Board disallowed certain expenses which did not meet the statutory standard of "honest, economical, and efficient management" (see *supra*, p. 12, n. 11).

and concession income was "other revenue" for determining mail pay need (R. 191), the Board relied upon the "broad statutory language referring to *all* other revenues," and the "desirability of reducing government support where the carrier has net income available to it from other sources to support its certificated operations * * *" (R. 193, italics in original). And, in holding that the entire profit on the sale of route 68 should be offset, the Board stated that it "would be contrary to the public interest to use public funds to subsidize a need which had already been covered by profits accruing from benefits under the certificate" (R. 198).

In its second decision, the Board again held that the entire profit on the sale of route 68 was "other revenue" within Section 406(b) (R. 261). However, the Board for the first time distinguished between the profit on the tangibles (equipment) and the intangibles (certificate), holding that the former but not the latter should be offset in calculating break-even need. It did so on the novel theory that Section 406(b) gives the Board "discretion" to "take in 'other revenue' in whole, in part, or not at all" (R. 262). We submit that this construction of the Act is unwarranted, and that under the Act the Board is required to include *all* other revenue, and has no discretion to take it in "in whole, in part, or not at all."

Section 406(b) defines the carrier's need for subsidy as an amount which, "together with all other revenue of the air carrier," is sufficient to enable the carrier

to meet the statutory objectives. In other words, the Board is directed to award subsidy in an amount which, when added to all the carrier's other, *i. e.*, non-mail pay, revenue, will provide it with funds to enable it to "maintain and continue the development of air transportation." The "bare uncomplicated situation is," as the Court of Appeals stated, "that when the carrier has substantial revenues from non-mail sources the margin of its need for mail pay is less" (R. 351-352). It was this "desirability of reducing government support where the carrier has net income available to it from other sources" that presumably led Congress to require the Board to offset *all* other revenue in determining subsidy need.

The source of such other revenue is immaterial; the significant fact is its amount. Western's need for subsidy was not increased because a portion of its revenues in 1947 was derived from the sale of a Government franchise. This revenue reduced the carrier's need for subsidy from the public treasure just as much as the revenue from the sale of the equipment used in operating under such franchise,¹⁹

¹⁹ In its second decision the Board, in offsetting the profit on the tangibles, stated that it saw no reason "why the carrier's need should be duplicated" therewith (R. 264). The Board consistently has offset profits on the sale of aircraft and equipment to reduce a carrier's subsidy need. *Chicago and Southern Air Lines, Mail Rates*, 3 C. A. B. 161, 172 (1941); *Colonial Airlines, Mail Rates*, 4 C. A. B. 71, 77 (1942); *Continental Air Lines, Mail Rates*, 8 C. A. B. 825, 843 (1947); *American Overseas Airlines, Mail Rates*, 9 C. A. B. 695, 706 (1948). In *Delta Air Lines, Mail Rates*, 9 C. A. B. 645, 654 (1948), the Board offset net income derived from an insurance settlement of the crash of one of the carrier's aircraft.

or from the operations of airport restaurant and slot machine concessions. When Congress used the words "all other revenue" in Section 406 (b), it did not mean "all or some part of such other revenue." (Brief in Nos. 222 and 223, pp. 30-45.)

The result of permitting the Board to ignore portions of a carrier's other revenue—for whatever reason—is to give the carrier a subsidy in excess of its needs. In the instant case the Board's holding in its first decision, not modified in its second decision (R. 268), was that Western "needed" subsidy which, together with *all* its other revenue, *i. e.*, the entire profit on the sale of route 68, would give it a 7 percent return for the years 1944 through 1948, and the Board awarded subsidy on that basis. By subsequently refusing to offset the profit on the intangibles, the Board in effect gave the carrier an additional subsidy of \$447,000. This results in a return of 14.76 percent for 1947, the year in which Western received the profit on the sale of route 68. The Board, however, had already determined that Western needed only a 7 percent return in that year. By thus giving Western a subsidy \$447,000 greater than it needed, the Board departed from the statutory requirement (see Point I, *supra*) that, subsidy cannot exceed the need of the carrier.

III.

WESTERN DID NOT "NEED" THE \$447,000 ADDITIONAL SUBSIDY MAIL PAY, AND THE AWARD THEREOF WAS NOT MADE ON THE BASIS OF WESTERN'S NEED

In refusing to offset the profit on the sale of the certificate, the Board did not find that Western

"needed" an additional subsidy of \$447,000, or that it "needed" a return of 14.76 percent in 1947 (see *supra*, p. 23). On the contrary, the Board merely stated that "* * * if we are to safeguard the incentive for voluntary route transfers, we cannot now refuse Western the right to retain at least some portion of the net profit from the sale of Route No. 68" (R. 264). But the Board's policy of encouraging voluntary route transfers does not establish the "need" of the transferring carrier to receive extra subsidy, and it is clear that Western did not need the additional subsidy awarded in this case.

In the first place, the Board's theory is predicated on an erroneous assumption. There is no question here as to Western's right to "retain" any portion of the proceeds of the sale of route 68.²⁰ As the Court of Appeals recognized, under a subsidy system "[n]one of the [carrier's] earned revenue is recaptured" (R. 351). Contrary to the Board's suggestion (R. 263), Western "keeps" every penny of the \$3,750,000 it received from the sale of route 68, including the \$1,099,000 profit. The sole question here is how

²⁰ The correctness of the Board's permitting Western to sell its certificate at a profit is questionable. Section 401(j) of the Act, which provides that no certificate shall confer any "proprietary" or "property" right on the holder, seemingly precludes such trafficking in certificates. Notes, 48 Columbia Law Review 88(1948), 61 Harvard Law Review 523 (1948); see dissent of Chairman Landis in the route transfer case, 8 C. A. B. at 333-334, 341-345.

much *additional* money Western is to receive as a subsidy from the public treasury. Or, putting it differently, the question is whether the Government is to duplicate through subsidy a portion of the profit previously realized by the carrier on the sale of its government franchise.

There is no showing that the extra subsidy was necessary to induce Western to make the transfer of route 68. Indeed, in its first decision the Board flatly found that (R. 198-199)—

There is no indication in the record that had Western been certain that the profit it would realize on the sale would be considered "other revenue" it would not have sold the route. In fact, it had no basis for believing otherwise when it negotiated the sale.

That finding has not been repudiated, and clearly is correct. As the Board itself recognized in its decision in the route transfer case (8 C. A. B. at 302-303) and concedes before this Court (Petition for Writ of Certiorari, No. 224, p. 11), it was Western's critical financial situation and its desire to dispose of a route not adapted to its long-term development as a regional carrier which prompted the sale. Moreover, Western could hardly have anticipated that the Board would exclude the profit from consideration for mail pay purposes. The clear warning in Chairman Landis' dissent in the transfer case that the transfer profit would reduce need mail pay

went unanswered in the majority opinion.²¹ The only Board decision that had dealt with the question up to that time included profits on the sale of a route in determining the carrier's need. *Inland Air Lines, Mail Rates*, 1 C. A. A. 155, 162-163 (1939). Thus it cannot fairly be said that Western "needed" this extra subsidy even in the special sense that, without it, the carrier would not have sold the route.

Nor is exclusion of such profits justified as a means of encouraging route transfers generally. For, as the Court of Appeals correctly held, the Act does not authorize the Board "to provide incentives to the industry generally," but restricts subsidy payments "to the need of each individual carrier to maintain and continue a development program of its own" (R. 349-350). And it is clear that the Board awarded Western additional subsidy "in order to encourage other carriers (not Western)" to effect route transfers.

In its second decision, the Board (R. 265)—

emphasized that our decision not to include the net profit from the sale of intangibles was reached *solely* because we are thus seeking to encourage improvement of the air route pat-

²¹Chairman Landis pointed out in his dissenting opinion that "under any theory" the \$1,500,000 was "revenue under section 406(b) of the Civil Aeronautics Act which the Board must take into consideration in fixing any need rate. The Board thus must in the last analysis charge the subsidy that Western will get and upon which it must depend with that amount, so that in the end Western's acquisition of \$1,500,000 becomes only a temporary advance against future subsidy payments." 8 C. A. B. 344-345.

tern through voluntary route transfers by other air carriers [emphasis added].

The Board also stated that it had permitted Western a "commercial profit" in selling route 68 to prevent "thwarting the improvement of the air pattern through voluntary action by the carriers," and that the incentive of profit from a route sale should be "preserved here" in order "to continue to encourage voluntary action by the carriers" (R. 263). In other words, the Board gave Western additional subsidy of \$447,000 in order to preserve the incentive for other carriers to sell their routes at some future date.²² The Act, however, makes the "need of each such air carrier" (emphasis added) the basis for awarding subsidy. Plainly, Western cannot be said to have needed the additional subsidy because other carriers might otherwise be discouraged from effecting future route transfers.

Furthermore, there is no basis for the Board's assumption that other carriers would refrain from making route adjustments if profits on such transfers were not to be duplicated with additional subsidy. As the Board noted in its first opinion (R. 199), the only major airline acquisition during the period 1947-1951—the purchase of American Overseas Airlines by Pan American Airways—was consummated on the basis of approximate book value, and raised no issue as to profit on intangibles. *North Atlantic*

²² Indeed, the Board recognized in its second decision that in approving the sale of route 68 it had not been "concerned * * * with the ultimate treatment of the profit which was to be realized by Western * * *" (R. 262; see R. 196).

Route Transfer Case, 11 C. A. B. 676, petitions to review dismissed for want of jurisdiction, *sub nom. Trans World Airlines v. Civil Aeronautics Board*, 184 F. 2d 66 (C. A. 2), certiorari denied, 340 U. S. 941. This fact, the Board stated, indicated that "there were sufficient incentives to negotiate this transaction on the part of both parties which outweighed the consideration of a profit," and that "the profit motive is [not] such a necessary consideration for the accomplishment of route transfers or mergers as Western would have us believe" (R. 199).²³

The Board has adequate authority to encourage route transfers through its other powers under the Act without having to resort to subsidies from the public treasury to accomplish this end. The Act requires carriers claiming subsidy to meet the standard of "honest, economical and efficient management." Retention of a route not economically adapted to the carrier's operations constitutes a failure of "economical and efficient management" just as much as operation of an excessive number of

²³ Whatever significance the granting of additional subsidy once may have had as a means of encouraging route transfers, it appears to be of diminishing importance today. For more and more of the major domestic carriers have, as they achieved economic self-sufficiency, shifted from a need to a service basis. Civil Aeronautics Board, *Administrative Separation of Subsidy from Total Mail Payments to United States Air Carriers*, September 1953 Revision, p. 3. Subsidy, of course, can be used to encourage route transfers only as long as the carrier is on a need rate.

flights,²⁴ payment of excessive salaries,²⁵ retention of unnecessary aircraft,²⁶ or unduly high maintenance charges,²⁷ The Board has reduced subsidy payments to take account of the foregoing management inefficiencies. There is no reason why similar adjustments in subsidy mail pay cannot and should not be made with respect to uneconomical routes that a carrier refuses to relinquish. Since Western had taken the position in the route transfer case that it no longer could operate Route 68 effectively unless it went into the trans-continental field and acquired substantial additional equipment which it then was not in a position to acquire, retention of the route under those circumstances would itself have constituted a failure of "economical and efficient" management.

We think the complete answer was given by the Board itself in its first decision. In reply to Western's argument that inclusion of the profit as "other revenue" would adversely affect carriers' incentives voluntarily to adjust route patterns, the Board stated:

²⁴ *Capital Airlines, Mail Rates*, 10 C. A. B. 705, 708-712.

²⁵ *Pioneer Air Lines, Mail Rates*, 8 C. A. B. 175, 185; *Trans-Texas Airways, Mail Rates*, 12 C. A. B. 101, 110.

²⁶ In the instant case, Western "moved quickly" to reduce the size of its fleet of DC-4 aircraft following a "rapid drop in traffic volume" in the fall and winter of 1946-1947 (R. 63-64).

²⁷ *Northeast Airlines, Mail Rates*, 9 C. A. B. 291, 296-304. In the instant case the Board disallowed certain excessive maintenance expenditures by Western (R. 212).

The incentive of a carrier wishing to dispose of a route or to merge is to correct a situation which is inimical to its best interests, such as the operation of an uneconomical route that will mitigate against its over reaching self-sufficiency. The incentive to divest itself of such a [uneconomical] route should be reinforced by the realization that *subsidy mail pay will not be forthcoming to perpetuate an uneconomic route pattern* [R. 198, emphasis added].

Indeed, the Board's settled policy to "reduce the extent of their [carriers'] dependence upon compensation from the Government,"²⁸ which the Board reasserted in its first decision (R. 193), requires such a result.

The Board also can effect desirable changes in the route pattern through its power under Section 401 (h) (*supra*, p. 3) to "alter, amend, modify, or suspend" any certificate, in whole or in part, "if the public convenience and necessity so require." Pursuant thereto the Board recently suspended the authority of two trunkline carriers to serve particular points authorized under their certificates in order to allow local carriers to serve the same places. *Western Air Lines v. Civil Aeronautics Board*, 196 F. 2d 933 (C. A. 9), certiorari denied, 344 U. S. 875; *United Air Lines v. Civil Aeronautics Board*, 198 F. 2d 100

²⁸ *Pan American-Grace Airways, Mail Rates*, 3 C. A. B. 550, 589 (1942).

(C. A. 7). Furthermore, appropriate mergers and consolidations, which the Board has not hesitated to suggest in the past,²⁹ afford another method of accomplishing route alterations without any drain on the public purse.

We submit that the Board had no basis, evidentiary or otherwise, for a conclusion that Western needed the additional subsidy of \$447,000. In its first opinion the Board clearly recognized that fact. But in the second opinion the Board shifted from the statutory test of need to the erroneous policy concept that having allowed Western a "commercial profit" in the route transfer case, it should permit the carrier to "retain" some of such profit. The Act, however, requires that *all* other revenue be taken into account in determining need, and confers no discretion upon the Board to offset such other revenue "in whole, in part, or not at all" (R. 262). In awarding Western an additional \$447,000 subsidy to encourage changes in the route pattern, the Board exceeded its statutory authority.

²⁹ See the Board's show cause order suggesting the combination of Continental Air Lines and Mid-Continent Airlines. Order No. E-5803, Docket No. 5173, October 23, 1951. The proceeding was dismissed following the proposed voluntary merger of Mid-Continent and Braniff Airways. Order E-6107.

A recent comment suggests a possible merger program for the airlines. 60 Yale L. J. 1196, 1213-1217 (1951).

CONCLUSION

The judgment of the Court of Appeals should be affirmed.

Respectfully submitted,

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DECEMBER 1953.

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JUL 31 1953

HAROLD B. WILLEY, CLERK

IN THE
Supreme Court of the United States

October Term, 1953

No. 225

WESTERN AIR LINES, INC.,

Petitioner,

vs.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMERFIELD,
POSTMASTER GENERAL OF THE UNITED STATES, AND
THE UNITED STATES OF AMERICA, ON BEHALF OF THE
POSTMASTER GENERAL,*Respondents.*

CIVIL AERONAUTICS BOARD,

Petitioner,

vs.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL OF THE
UNITED STATES; THE UNITED STATES OF AMERICA, ON
BEHALF OF THE POSTMASTER GENERAL; AND WESTERN
AIR LINES, INC.,*Respondents.*

Petition of Western Air Lines, Inc., for a Writ of
Certiorari to the United States Court of Appeals
for the District of Columbia Circuit.

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IN THE
Supreme Court of the United States

October Term, 1953

No. _____

WESTERN AIR LINES, INC.,

Petitioner,

vs.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMERFIELD,
POSTMASTER GENERAL OF THE UNITED STATES, AND
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POSTMASTER GENERAL,

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CIVIL AERONAUTICS BOARD,

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vs.

ARTHUR E. SUMMERFIELD, POSTMASTER GENERAL OF THE
UNITED STATES; THE UNITED STATES OF AMERICA, ON
BEHALF OF THE POSTMASTER GENERAL; AND WESTERN
AIR LINES, INC.,

Respondents.

**Petition of Western Air Lines, Inc., for a Writ of
Certiorari to the United States Court of Appeals
for the District of Columbia Circuit.**

Western Air Lines, Inc., respectfully petitions that a
Writ of Certiorari issue to review the judgment of the
United States Court of Appeals for the District of
Columbia Circuit in *Summerfield v. Civil Aeronautics
Board*, No. 11259, and *Western Air Lines v. Civil Aero-
nautics Board*, No. 11324.

Opinions Below.

The opinion of the Court of Appeals,¹ which is not yet reported, appears in the record of this proceeding commencing at page 341.²

The opinions of the Board which were reviewed by the Court of Appeals are included in the record of this proceeding commencing separately at pages 183, 258 and 333.

Jurisdictional Statement.

The judgment of the Court of Appeals was entered on May 4, 1953 [R. 354]. The jurisdiction of this Court is invoked under Subsection 1254(1) of Title 28, U. S. Code, and Subsection 646(f) of Title 49, U. S. Code.

Summary and Statement of Matter Involved.

This case concerns the fair and reasonable rate of compensation which Western is entitled to receive for transporting mail by aircraft during the period from May 1, 1944, through December 31, 1948. The dispute centers upon the language employed by the Congress in Subsection 406(b) of the Act (49 U. S. Code, Sec. 486).

Subsection 406(a) of the Act is the enabling provision which empowers the Board to fix and determine fair and reasonable rates of compensation for the transportation of mail by aircraft.

¹For convenience, the United States Court of Appeals for the District of Columbia Circuit will be referred to as the "Court of Appeals," Western Air Lines, Inc., as "Western," the Civil Aeronautics Board as the "Board," and the Civil Aeronautics Act as the "Act."

²For convenience also, the opinion of the Court of Appeals is included in this petition as Appendix A.

Subsection 406(b) sets forth guides to aid the Board in determining the rates.

The legal points necessitating this petition involve the proper construction of (1) the statutory expression "shall take into consideration, among other factors" and (2) the statutory expression "all other revenue of the carrier," appearing in Subsection 406(b).

The pertinent facts in the case are simple. On April 26, 1944, Western filed a petition under Subsection 406(a) of the Act for an increase in the rate of its compensation for carrying the mail [R. 15]. That petition was acted upon by the Board for the first time late in 1948, more than four years after the filing date [R. 54]. During the long interim, Western sold, with Board approval,³ one of its air routes and certain equipment and properties used in connection with the route at a net book profit of approximately \$1,000,000.00 [R. 196]. Western also experienced during the delay period, among other income, net profits of approximately \$88,000.00 from the operation of slot-machine concessions in Las Vegas, Nevada, and restaurants and cafeterias [R. 192].

In 1951 the Board finally awarded to Western the sum of \$3,917,361.00 as its total compensation for the transportation of mail in the past period, May 1, 1944, through December 31, 1948 [R. 338]. In arriving at this determination, the Board ruled that Western's net adjusted profit from the sale of the route in 1947 and Western's net profits from the operation of slot machines,

³*United-Western, Acquisition of Air Carrier Property*, 8 C. A. B. 298 (1947).

restaurants and canteens were "other revenue" within the meaning of Subsection 406(b) of the Act [R. 191-200, 261, 266-267]. However, the Board chose to allow Western to retain a part of the profit from the route sale by not offsetting it against Western's mail compensation on the policy ground that voluntary route adjustments would be encouraged [R. 262-265].

The Court of Appeals agreed with the Board's application of the statutory expression "other revenue" but ruled that the Board is without power under the statute to fix individual rates of compensation for the transportation of mail other than on the basis of the particular carrier's specific *need* for compensation, regardless of other public interest factors [R. 349-450].

Statutes Involved.

Section 406 of the Civil Aeronautics Act (52 Stat. 998; 49 U. S. Code, Sec. 486) is set forth in Appendix B to this petition. Other sections of the Act are only indirectly involved and will be set forth at the places where they are mentioned.

Questions Presented.

1. Does the statutory expression "shall take into consideration, among other factors" in Subsection 406(b) bestow on the Board judicial discretion with respect to the weight it shall give to each factor material to the process of rate-making?

2. Does the statutory expression "all other revenue of the air carrier" in Subsection 406(b) of the Act embrace more than revenue derived from the carriage of passengers and property?

3. Does the statutory expression "all other revenue of the air carrier" in Subsection 406(b) include the net profit from the sale of an air route and related equipment?

4. Does the statutory expression "all other revenue of the air carrier" in Subsection 406(b) include an air carrier's net profit from the operation of slot machines, restaurants or canteens?

Specifications of Errors to Be Urged.

The Court of Appeals erred in holding:

1. That the Board followed a concept of its power unauthorized by Section 406 in not offsetting all of Western's profit from the route sale against Western's mail compensation.

2. That Western's net adjusted book profit from the sale of an air route and equipment used in connection with the route constituted "other revenue" within the meaning of Subsection 406(b).

3. That Western's net profit from the operation of slot machines, restaurants and canteens constituted "other revenue" within the meaning of Subsection 406(b).

REASONS FOR GRANTING THE WRIT.

- A. It Is Essential to the Proper Regulation of the Air Transportation Industry to Have the Statutory Term "Shall Take Into Consideration" Interpreted by This Court.

This case involves important considerations of public interest. Crucial questions of federal law—the interpretation of a rate-making statute—going to the very core of the regulatory scheme adopted by the Congress for the indispensable air transportation industry are at stake. The vital issues have not been presented to the courts before.

Stripped down to the essentials pertinent to the proper construction of "shall take into consideration, among other factors," Subsection 406(b) reads:

" . . . In determining the rate in each case, the Board *shall take into consideration, among other factors, . . . the need of each such air carrier for compensation for the transportation of mail sufficient . . . , together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.*"

The Board consistently has taken the position that the term "shall take into consideration," as used in Subsection 406(b), only requires the Board to *consider* the factors enumerated, among others, leaving to the

Board the discretionary right of doing what appears to be proper.⁴ This contemplates, of course, that the discretion will be exercised judiciously. Western agrees with the Board's interpretation.

The Postmaster General takes the opposite view. He contends that after the Board has considered all of the other revenue of a carrier (which the Postmaster General thinks is all income) the Board has no discretion but must apply that revenue in reduction of the mail compensation regardless of what public interest considerations might exist for doing otherwise.⁵

Apparently the Court of Appeals adopted the Postmaster General's theory, although the opinion of the lower court, written by Circuit Judge Prettyman is, at best, confusing.⁶ And, this confusion is somewhat confounded by the dissenting opinion of Circuit Judge Prettyman in the companion case below, *Summerfield v. Civil Aero-*

⁴In its opinion and order dated June 26, 1951, the Board stated:

"While we are required by the Act to 'take into consideration' the 'need' of the carrier for mail compensation together with 'all other revenue,' we do not understand the language of section 406(b) as requiring us to reduce the carrier's mail pay 'need' with any part of such 'other revenue.' This is a matter within our discretion." [R. 262.]

⁵In his Petition to Reconsider before the Board dated July 27, 1951, the Postmaster General stated:

"The mail rate section (406(b)) of the Civil Aeronautics Act does not permit the Board discretion to disregard the net revenues derived from the sale of a route certificate when determining the carrier's need for subsidy mail compensation." [R. 282.]

⁶The Court of Appeals in its opinion below stated:

"Thus we think that, while the so-called 'need' provision of the statute, above quoted, does provide for the payment of sums sufficient to enable the carrier under consideration to maintain and continue development of air transportation, such payments are restricted to the need of each individual carrier to maintain and continue a development program of its own." [R. 349-350.]

navitics Board, No. 11351, in which this irreconcilable statement is found on page 10 of the printed opinion:

"I am so convinced of the soundness of a complete separation of this foreign rate from the domestic operation, that I would have to agree with the Board that *the elastic statutory phrase 'take into consideration' is sufficiently flexible to permit the omission of domestic earnings from the foreign calculation, even after such earnings are taken into consideration.*"⁷

So long as uncertainty attaches to the meaning of "shall take into consideration" in consequence of divergent views entertained by the Board (shared by the industry) and the Postmaster General, coupled with a hazy majority opinion below, contrasting with the conflicting dissenting opinion written by the same Circuit Judge, uncertainty in the administration of a vital part of the Act—the rate-making part—will prevail. And, uncertainty breeds instability, which was the principal evil that the Act was designed to remove.

Although this case concerns only compensation for carrying the mail, the meaning of the term here under discussion has a direct bearing on the Board's control of passenger and property tariffs. Exactly the same phrase is employed in Subsection 1002(e),⁸ which sets

⁷Emphasis in quoted material added throughout unless otherwise noted.

⁸Section 1002(e) (49 U. S. Code, Section 642) reads in part:

"In exercising and performing its powers and duties with respect to the determination of rates for the carriage of persons or property, the Board *shall take into consideration, among other factors—*

* * * * *

(5) The need of each air carrier for revenue sufficient to enable such air carrier, under honest, economical, and efficient management, to provide adequate and efficient air carrier service."

forth some of the factors which the Board is required to consider in exercising its powers with respect to passenger and property tariffs.

If the Board lack judicial discretion under Subsection 406(b) relating to mail compensation, as here claimed by the Postmaster General and probably approved by the Court of Appeals, the Board necessarily lacks judicial discretion under Subsection 1002(e). If this be so, disaster could easily engulf the air transportation industry, as nowhere is sound discretion needed more than in the passenger and property tariff-fixing power of the Board—the very jugular vein of air transportation.

If the Board's rate-making power be stripped of discretion, as it would be under the Postmaster General's philosophy and the probable ruling of the Court of Appeals, the Board's ability to respond to its duties under Section 2 of the Act,⁹ which relates to the encouragement

⁹Section 2 (49 U. S. Code, Section 402) reads:

"In the exercise and performance of its powers and duties under this chapter, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

"(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

"(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriage;

"(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

"(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce

and development of air transportation, would be shackled. No provision in the Act, not even the authority to grant, amend and modify route certificates under Section 401, gives the Board as much power to foster the development of air transportation as does its rate-making power, both mail and passenger, provided, but only provided, the Board be cloaked with reasonable judicial discretion. That discretion exists only if the term "shall take into consideration" be construed here as it should be.

Innumerable examples of the grave importance of this issue to the continuing long-range development of the vital air transportation industry could be listed, but none is as pointed as the example found in this case. In exercising what it thought was its discretionary power in offsetting or not offsetting other revenue after having taken that other revenue into consideration, the Board declared:

"In order to avoid the danger of confining the present air pattern to a rigid mold, and to continue to encourage voluntary action by the carriers, we believe that the incentive of profit which may be derived from the sale of a route . . . should be preserved here." [R. 263.]

The exigent significance of this is underscored by reference to Section 401 of the Act (49 U. S. Code, Sec. 481). Subsection 401(e), commonly referred to as the "grandfather clause," established a method for automatic issuance of certificates covering air routes in existence when

of the United States, of the Postal Service, and of the national defense;

"(e) The regulation of air commerce in such manner as to best promote its development and safety; and

"(f) The encouragement and development of civil aeronautics."

the Act came into being. Many of those routes had grown up like Topsy, and at least some of them have proved to be ill-advised. In addition, experience has proved that some of the new certificates since granted by the Board under Section 401(d) likewise are ill-advised or could be operated more economically and more effectively by some other carrier. Still the Board has no direct power under the Act to force an abandonment of a route, a transfer of a route from one carrier to another or the merger of two or more carriers. With the discretionary power to allow a selling carrier to retain the nonrecurring profit (assuming this to be revenue required to be heeded under Sub. 406(b)) resulting from the voluntary sale of a route, great impetus will be given to a voluntary and beneficial realignment of the air route pattern. If that profit must be or might be drained off as an offset against the mail compensation, all incentive would be destroyed.

The essence of the opinion of the Court of Appeals is that lacking a showing of need the Board is powerless to fix a rate of compensation for transporting the mail exceeding a naked compensatory rate. But this theory gives no effect to the statutory language "among other factors." On the contrary, the theory fetters the Board by a literal interpretation which is completely at odds with the flexibility intended by the Congress. The expression "among other factors" means simply that the Board within the limits of sound discretion may fix the rate on the basis of factors other than the "need" of the air carrier or on the basis of that "need" as modified by other factors or on the basis of that "need" alone. The Court of Appeals does not challenge or deny the force of the Board's reason for doing what it did in this case but rests its decision

on a construction of the statute which, contrary to the terms of the statute, denies the Board discretionary power and restricts mail payments to the need of the air carrier.

B. It Is of Vital Importance to the Air Transportation Industry, to the Civil Aeronautics Board and to the Postmaster General to Have the Meaning of the Statutory Expression "All Other Revenue of the Air Carrier" Settled.

The Postmaster General has interpreted Subsection 406(b) to mean that all *income* of an air carrier, *regardless of source*, must be applied in reduction of or in the nature of an offset to the carrier's mail compensation.¹⁰

The Board has interpreted the subsection to mean that all *income* of an air carrier *from activities related to air carrier functions* should be considered in fixing the fair and reasonable rate of compensation for transporting mail.¹¹

Western adheres to the position that the "all other revenue" required to be considered by the Board under Subsection 406(b) is limited to revenue derived from the transportation of persons and property.

¹⁰On page 21 of the Postmaster General's Brief to the Court of Appeals, this statement is made:

"Moreover, it is evident that the carrier's actual need can be determined only by a comparison of its actual income *from all sources*, with the amount of income determined by the Board to be sufficient to enable the carrier to perform its transportation functions properly and to receive a fair return on its investment."

¹¹In its opinion of November 24, 1950, the Board stated:

"Where the activity from which the income arose is related to the air carrier functions, such income should be considered as 'other revenue.'" [R. 193.]

It is self-evident that one of the three theories is right. No other interpretation of the subsection, stemming from reason, can be conceived.

Although the language of the Court of Appeals in the opinion under attack is far from clear, it is probable that the Court intended to place its imprimatur on the theory espoused by the Board.

Until the issue has been finalized no air carrier except those enjoying a so-called "compensatory" mail rate, can plan or budget its future. Until these carriers know with certainty what type of income will be and what type of income will not be applied in reduction of their mail compensation, they cannot create plans to expand their activities into broader fields, related or unrelated, in augmentation of their income or as a shield against a depressed air traffic period or make plans to merge or sell any of their routes to other air carriers.

If the Board's theory—the middle road—be given court approval, the industry still will be in a state of confusion unless the related activities, the income from which would be applied in reduction of the mail compensation, are defined with sufficient accuracy to enable the carriers as well as the Board and the Postmaster General to determine what ventures or activities will be within and what will be without the offsetting area. It is not right and it is contrary to the American conception of fairness to allow a condition to exist under which a carrier does not know and cannot determine whether the profit, if any, from a certain course of conduct or from a certain venture may be retained or will be applied in reduction of its mail compensation. So, if the Board's middle ground philosophy be accorded court

approval, the term "related activities" will have to be defined.

If either the Board's theory or the Postmaster General's theory be approved, it is essential that the industry know, and the Board and the Postmaster General must be told with authority, whether or not a loss from an act or a venture will be underwritten through increased mail compensation. If a profit from a particular venture be subject to offset it would be in violation of all sense of justness to hold that a loss from the same venture would not be subject to recoupment. But the Board thinks otherwise,¹² so the issue must be resolved in court.

C. The Decision of the Court of Appeals Is Not Good Law and Must Be Reversed.

The opinion of the Court of Appeals makes bad law and adds more ambiguity to important provisions of the Act which were and still are in need of clarification. Unless and until reversed by this Court or corrected by an act of Congress, the Board will be bound in its future administration of the Act by the opinion below. In the meantime, the American Flag air transportation industry will suffer to the irreparable damage of the public welfare.

¹²On page 16 of its brief to the Court of Appeals, the Board stated:

" . . . Further, even if a particular related air carrier activity is of such nature that losses will not be underwritten, we still see no reason why profits therefrom should not be offset against the carrier's need for subsidy."

1. **The Court of Appeals Misconstrued the Meaning of "Shall Take Into Consideration," Contrary to the Plain Intent of the Congress.**

Subsection 406(b) requires that the Board, in determining the rate in each case, "*shall take into consideration*" certain enumerated rate-making elements, "*among other factors.*"

The Postmaster General argued below that the term "shall take into consideration" charged the Board with a mandatory duty rather than granting a discretionary power.¹³ The Court of Appeals evidently accepted this argument, although Circuit Judge Prettyman, the author of the opinion in this case, adopted a contrary view in his dissenting opinion in the companion *Chicago & Southern* case, as already has been noted in this petition.

Consistently, the Board has interpreted "shall take into consideration" to mean what simple semantics would have it mean, the discretionary right of doing what good judgment dictates—offsetting or not offsetting other revenue against mail compensation—in accordance with the circumstances that might prevail in each situation under consideration. The Board has always thought that the

¹³In his Petition to Reconsider before the Board dated July 27, 1951, the Postmaster General stated:

" . . . in the consideration of whether the development of air transportation requires a subsidy to a particular carrier in addition to compensation for services rendered, as directed by the same section, the Board has *no discretion* under such section but must take into account all other revenue of such carrier obtained from all sources."

only mandate which it was required to meet was *to consider* and then act affirmatively or negatively in response to its judicial discretion. Western agrees.

Had the Congress intended that the Board *had* to offset all other revenue it would have been very simple to use language that could not have been misconstrued, assuming that there be any justification for the obvious misconstruction placed on the term by the Postmaster General. Moreover, had the Congress intended that "shall take into consideration" would require positive action beyond giving consideration it is not likely that the term would be followed by the clause "among other factors" without identifying those other factors.

(a) ESTABLISHED PRINCIPLES OF RATE-MAKING DEMAND THAT THE BOARD HAVE CONSIDERABLE FLEXIBILITY.

This Court has recognized that the process of rate-making is one primarily within the exclusive province of the expert governmental agency having the power to fix rates. In *Board of Trade v. United States*, 314 U. S. 534 (1942), in an opinion delivered by Mr. Justice Frankfurter, this Court declared:

"The process of rate-making is essentially empiric. The stuff of the process is fluid and changing—the resultant of factors that must be valued as well as weighed. Congress had therefore delegated the enforcement of transportation policy to a permanent expert body and has charged it with the duty of being responsive to the dynamic character of transportation problems." (P. 546.)

In connection with the provisions of Section 15(a)(2) of the Interstate Commerce Act, Mr. Justice Douglas in the case of *New York v. United States*, 331 U. S. 284 (1947), stated:

“The balancing and weighing of these interests is a delicate task . . . There may be differences of opinion concerning the weight to be given those factors . . . But their significance is for the Commission to determine; and, though we had doubts, we would usurp the administrative function of the Commission if we overruled it and substituted our own appraisal of these factors.” (Pp. 347, 349.)

The general principle was reiterated by Mr. Justice Black in *Baltimore & Ohio Railroad Company v. United States*, 345 U. S. 146 (1953), in this fashion:

“This mere sample of factors that have to be considered in rate cases demonstrates *the absolute necessity for considerable flexibility in rate-making* . . . Commission power to adjust rates to meet public needs is implicit in the congressional plan for a nationally integrated railroad system.” (P. 152.)

(b) THE WORDS “TAKE INTO CONSIDERATION” IMPOSE NO OBLIGATION ON THE BOARD TO ACT.

In *United States v. Interstate Commerce Commission*, 88 F. 2d 780 (1937), certiorari denied, 300 U. S. 684 (1937), the United States Court of Appeals for the District of Columbia construed the words “due consideration,” appearing in Section 15(a)(2) of the Interstate Commerce Act, in this manner:

“The mandate of the act . . . is that the Commission shall give ‘due consideration.’ *To give due consideration to a particular factor necessarily*

means to give such weight or significance to it as under the circumstances it seems to merit, and this, of course, involves discretion; and, as has been said many times, judicial discretion." (P. 783.)

- (c) THE WORDS "AMONG OTHER FACTORS" PERMIT THE BOARD TO CONSIDER AND ACT UPON FACTORS OTHER THAN ARE SET FORTH IN THE STATUTE.

In *United States v. Interstate Commerce Commission*, 88 F. 2d 780 (1937), certiorari denied, 300 U. S. 684 (1937), the United States Court of Appeals for the District of Columbia had this to say:

"Putting aside all questions of relative importance of the various elements of rate making—because the controlling facts in each case necessarily vary—there can be no doubt that in prescribing reasonable rates the Commission is required to take into consideration, *among other factors*, first, the effect of the rate on the movement of traffic; second, public need of adequate low-cost service; third, the carrier's need of sufficient revenue to enable it to give such service. This, we think, is the clear mandate of the statute. But the weight to be given to these several factors is left to the discretion of the Commission, *as is also the weight to be given the other and unnamed factors which of necessity vary in substance according to the facts.*" (P. 782, first italics in original.)

This broad sweep of discretion to choose the standard or standards upon which to fix rates was reiterated by the United States District Court for the Eastern District of Kentucky in *Chicago B. & Q. R. Co. v. United States*, 60 F. Supp. 580 (1945):

"Congress has not prescribed the 'other factors' to be considered by the Commission in the exercise

of its power to fix just and reasonable rates. *The determination of the issue of fact in respect to reasonableness as well as the choice of the standard upon which the determination is to be made in each particular case, is left to the informed judgment of the Commission . . .*" (P. 585.)

The Board in this case rested its holding upon the determination that there was a public need for readjustment of the air route pattern through route transfers between air carriers, in order to correct undesirable and uneconomic route structures existing in the air transportation system of this country. Recognizing that it is without power to compel air carriers to transfer routes or to merge, the Board here fixed upon a policy which would preserve the profit incentive to voluntary route adjustments.

The Court of Appeals did not deny, nor could it have denied, the existence of a public need for voluntary route transfers. That is within the exclusive province of the Board to determine. What the Court of Appeals denied was the Board's statutory power to encourage carriers, including Western, to transfer routes, by providing incentives in fixing mail pay.

The implementation of the public interest factors in Section 2 of the Act,¹⁴ in fixing rates, is not a new concept. In *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949), this Court, in an opinion delivered by Mr. Justice Douglas, stated:

" . . . §406(b) authorizes the Board to fix rates for 'classes of air carrier.' It is plain that the uni-

¹⁴Section 2 is quoted in full in footnote 9, pages 9-10.

form rate for the class is an important regulatory device. For §2(d) of the Act looks to the sound development of an air transportation system through competition. A uniform rate forces carriers within a given class to compete in securing revenue and in reducing or controlling costs." (Pp. 606-607.)

The right to encourage competition through uniform mail rates, which do not necessarily reflect or correspond to the individual carriers need for compensation, is not different from the right to encourage improvement of route structures and betterment of economic conditions in the industry through the mail rate.

It is fitting that the Board be afforded ample flexibility in its rate-making power to permit it to accomplish the broad purposes of the Act and not alone those purposes specified in Subsection 406(b).

2. The Court of Appeals Failed to Meet the Issue of the Meaning of "All Other Revenue of the Air Carrier" in Subsection 406(b).

Not once did the Court of Appeals discuss the meaning of "revenue." The Court's singular justification for not replying to Western's contentions regarding the meaning of "revenue" was that the rate period had passed and everyone knew Western had these special amounts of income.¹⁵

¹⁵The Court of Appeals in its opinion below stated:

"The Board knew, and we all know, that Western had in this period this \$1,000,000, or thereabouts, in profit.

* * * * *

"It seems to us that under this statute the Board, in fixing a rate of compensation for a past period, may view the facts as it knows the facts to be, that in determining 'need' it is not compelled to ignore that which it knows." [R. 347-348.]

In taking for granted without analysis the meaning of "all other revenue," the Court of Appeals not only ignored Western's arguments but ignored the elementary rules of statutory construction.

Mr. Justice Sutherland in *Porto Rico v. Shell Co.*, 302 U. S. 253 (1937), made this declaration:

"Words generally have different shades of meaning, and are to be construed if reasonably possible to effectuate the intent of the lawmakers; and this meaning in particular instances is to be arrived at not only by a consideration of the words themselves, but by considering as well, the context, the purposes of the law, and the circumstances under which the words were employed." (P. 258.)

Evidently the Court of Appeals was much impressed with the word "need," together with which "all other revenue of the air carrier" is to be considered by the Board. But the word "need," which is found in the same context in all Federal statutes pertaining to interstate common carriers and their rates,¹⁶ is no more than a shorthand, legislative method of expressing the detailed cost analysis of the results of operations, pervading every rate-making proceeding.

The Court of Appeals admitted that its construction would complicate the Board's duty under the statute and would give rise to unforeseen and inequitable differences between air carriers [R. 348]. The Congress hardly could have intended such a result.

¹⁶E. g., 49 U. S. Code, Subsections 15a(2), 316(i), 907(f).

- (a) WESTERN'S CONTENTIONS ARE PERSUASIVE AND DEMONSTRATE THAT "ALL OTHER REVENUE" IS LIMITED TO REVENUE OF THE AIR CARRIER FROM THE CARRIAGE OF PASSENGERS AND PROPERTY.
- (1) *The Congress Did Not Intend in Section 406 to Depart From the Customary Pattern of Fixing Rates Prospectively, Thus Limiting the Meaning of "Revenue."*

The manifest intent of the Congress in Section 406 is that rates of compensation for the transportation of mail by aircraft will be fixed prospectively. The Board at all times since its creation has acted on this premise. And, it has been only where lack of expedition in a mail rate-making proceeding has occurred, as in this case, that the Board has been confronted with fixing a retroactive rate.

This design of the Act is an important, if not the controlling, consideration in the proper construction of the statute. Income which is susceptible and capable of being forecast by the Board is "revenue" which the Board must take into consideration. Conversely, income which is not susceptible or capable of being forecast by the Board is *not* "revenue" which the Board must take into consideration. A nonrecurring, sporadic capital gain (or loss), such as from the sale of a route, is not susceptible of anticipation and therefore may not be deemed "revenue" (or expense) in the Board's rate-making.

Revenue derived from the transportation of persons and property is the only type of income which can be forecast by the Board with expertness and within range of fairness. During any period projected into the future every certificated air carrier, except the few holding

limited certificates, is certain to derive some revenue from the transportation of passengers and property—the only variance being the volume—and the Board members, being experts in air transportation, are qualified to estimate the revenue from these two sources.

But even though the phrase “all other revenue” be tortured improperly to mean *all other income* from whatever source and of whatever nature, it could only mean the type of income which would lend itself to foresight estimates—rather than hindsight knowledge. This in turn signifies that the term, even as thus twisted, could only embrace reasonably anticipative earnings from normal activities and operations. It could not possibly include a nonrecurring profit, such as the sale of a route certificate or capital assets, for instance, or some type of a “wind-fall,” if a colloquialism will be permitted, such as a substantial book profit from an insured casualty.

It is certain that the Congress would not have burdened the Board members, experts in air transportation but not in other fields of business ventures, with the duty of having to estimate what an air carrier might earn during a future period from running a restaurant, maintaining a dry goods store or operating slot machines and oil wells.

(2) *The Term “Revenue” Has a Restricted Meaning and Was Used in a Restricted Sense in Subsection 406(b).*

The word “revenue” is used only twice in the Act. The second time is in Subsection 1002(e), which reads in part:

“In exercising and performing its powers and duties with respect to the determination of rates

for the *carriage of persons or property*, the Board shall take into consideration, among other factors—

* * * * *

“(5) The need of each air carrier for *revenue*, sufficient to enable such air carrier, under honest, economical, and efficient management, to provide adequate and efficient air carrier service.”

The word “revenue” in Subsection 1002(e)(5) means revenue derived from the rates charged for the carriage of persons and property. The word cannot possibly mean anything more or anything else. It follows that the expression “other revenue” used in Subsection 406(b) cannot refer to any revenue other than the revenue referred to in Subsection 1002(e), because the term “revenue” is not used in any other section of the Act.

It is worthy of note that the other revenue required to be considered by the Board is “*revenue of the air carrier*.” An air carrier under Subsection 1(2) of the Act (49 U. S. Code, Sec. 401) is “any citizen of the United States who undertakes . . . to engage in air transportation.” Accordingly, in using the words “revenue of the air carrier” the Congress must have intended to mean the revenue which the air carrier would derive from being engaged in air transportation. Air transportation under Subsection 1(10) of the Act includes interstate air transportation, which in turn under Subsection 1(21) means *the carriage by aircraft of persons or property as a common carrier for compensation or the carriage of mail by aircraft*. Had Congress not intended to limit

other revenue, as used in Subsection 406(b), to the revenue referred to in Subsection 1002(e), it would have used language which would have been unequivocal.¹⁷

In *Interstate Commerce Commission v. Cincinnati, N. O. & T. P. R. Co.*, 167 U. S. 479 (1879), this Court at page 495 noted that the language by which the power to fix rates is granted is so often used and is so familiar to the legislative mind that it "is capable of . . . definite and exact statement."

(3) *The Board Has No Control Over the Amount of Income an Air Carrier Derives From Collateral or Incidental Activities.*

Under the Act the Board has control over and power to prescribe the revenue of air carrier *only* with reference to the three principal sources of air carrier income—passengers, property and mail. Section 1002 gives the Board the power to determine and prescribe the rates which an air carrier may charge for transporting passengers and property. Section 406 empowers the Board to determine and ~~fix~~ rates of compensation for transporting the mail. The Board has no power to determine the prices an air carrier shall charge or the amount of income an air carrier shall receive in connection with in-

¹⁷Mr. Justice Jackson, dissenting *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 600 (1949), gave recognition to the true meaning of the word "revenue," in this fashion:

"But Congress believed that, in the interest of the national defense and commercial aviation, it had to subsidize pioneering air lines and underwrite *revenues above those to be realized from passenger and cargo carriage.*" (P. 609.)

cidental or collateral activities, such as the operation of restaurants and slot machine concessions.

Since the Board has control over the revenues derived from transporting passengers and property and thus has the power to see to it that those revenues are productive of a reasonable return to the carrier in connection with the air transportation service it is required to maintain, it is altogether fitting that the Board should have the right to consider those revenues in fixing a fair and reasonable rate of compensation for transporting the mail. Since the Board does not have the power to determine the prices that an air carrier shall charge or receive in connection with its incidental or collateral activities, it is only proper that the income (or loss) from those sources should not be considered by the Board in arriving at a fair and reasonable rate of compensation for the transportation of mail.

Conclusion.

Three reasons, each involving considerations of compelling public interest, exist for issuing a writ of certiorari in this case:

1. The fair and legal administration of Section 406 of the Act—one of the paramount sections—requires a full and final interpretation by this Court;

2. The unresolved divergent constructions placed upon an essential part of Section 406 by the two governmental agencies most concerned with its administration will create continuous confusion and dissention in a utility of critical importance to the country; and

3. Unless corrected, the error of the Court of Appeals in upholding the Postmaster General's erroneous interpretation of "shall take into consideration" in this and its companion case, *Summerfield v. Civil Aeronautics Board*, and in approving the Board's fallacious interpretation of "all other revenue" will set in motion a chain of bad decisions by the Board, thereby hampering the continued development of air transportation.

Los Angeles, California, July 29, 1953.

Respectfully submitted,

HUGH W. DARLING,

DONALD K. HALL,

Attorneys for Petitioner Western Air Lines, Inc.

D. P. RENDA,

Of Counsel.

APPENDIX A.

UNITED STATES COURT OF APPEALS for the District of Columbia Circuit

No. 11259

Arthur E. Summerfield, Postmaster General of the United States, and The United States of America, on behalf of the Postmaster General, Petitioners, v. Civil Aeronautics Board, Respondent.

No. 11324

Western Air Lines, Inc., Petitioner, v. Civil Aeronautics Board, Respondent.

On Petitions for Review of Orders of the Civil Aeronautics Board. Decided May 4, 1953.

Mr. Daniel M. Friedman, Special Assistant to the Attorney General, Department of Justice, *pro hac vice*, by special leave of Court, with whom *Mr. Newell A. Clapp*, Acting Assistant Attorney General, Department of Justice, was on the brief, for petitioners in No. 11259. *Mr. Charles H. Weston*, Chief, Appellate Section of the Anti-trust Division, Department of Justice, and *Mr. William E. Kirk, Jr.*, Assistant United States Attorney at the time of argument, also entered appearances in behalf of the petitioners in No. 11259.

Mr. Hugh W. Darling for petitioner in No. 11324. *Mr. L. Welch Pogue* also entered an appearance in behalf of petitioner in No. 11324.

Mr. O. D. Ozment, Attorney, Civil Aeronautics Board, with whom *Mr. Emory T. Nunneley, Jr.*, General Counsel,

Civil Aeronautics Board, was on the brief, for respondent, Mr. John H. Wanner, Associate General Counsel, Civil Aeronautics Board, also entered an appearance in behalf of respondent.

Before PRETTYMAN, PROCTOR and BAZELON, Circuit Judges.

PRETTYMAN, *Circuit Judge*: These cases concern orders of the Civil Aeronautics Board which fixed the compensation of Western Air Lines for the transportation of mail from May, 1944, through December, 1948. The dispute revolves about Section 406 of the Civil Aeronautics Act.¹ The proper treatment of several matters is involved.

Principally the petitions concern the treatment of the profit derived by Western from the sale to United Air Lines of a certificate for an air route and certain equipment used in connection therewith. Prior to September 15, 1947, Western owned a certificate for Route 68—between Los Angeles and Denver. After a hearing the Civil Aeronautics Board approved the sale of the route and the equipment to United Air Lines² for a total price of \$3,750,000. Of this \$722,000³ was then computed as profit on the sale of tangibles and \$447,000 as profit on the sale of intangibles. The Board decided that the transfer of the route at the amount to be paid by United was in the public interest, because the profit on the transaction would provide the necessary incentive for Western

¹52 Stat. 998 (1938), as amended, 49 U. S. C. A. §486.

²United-Western, Acquisition Air Carrier Property, 8 C. A. B. 298 (1947).

³Later recomputed to be \$648,102.

to make a sale and the purchasing carrier could operate the property to greater advantage to the public. The Board acted upon the premise that it has no power to force a carrier against its will to transfer property to another carrier; its only power to influence such transfers is the power of inducement. It decided that a profit on a sale would be such an inducement. Hence it approved the sale.

When the Board came, in the present proceeding, to the determination of compensation to Western for the transportation of mail, a problem arose as to the treatment of this profit in the computations.

The statute, in pertinent part, provides:

“(a) The Board is empowered and directed * * * to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft * * *.

“(b) * * * In determining the rate in each case, the Board shall take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.”⁴

⁴*Supra*, note 1.

The statutory language which is critical in the present dispute is "the need of each such air carrier for compensation * * * sufficient * * *, together with all other revenue of the air carrier, * * * to maintain and continue the development of air transportation."⁵

Perhaps the problem is made clearer by use of a little simple arithmetic. If a carrier has \$1,000,000 in revenue and \$1,300,000 in expenses, obviously it needs \$300,000 to break even; the "break even need." Then it needs a return on its investment and some working capital; let us say \$200,000 for those needs. The statute says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation. Let us suppose that for the latter purpose the carrier needs another \$100,000. In sum the carrier needs \$600,000. Now, obviously, in this calculation the greater the amount of the carrier's existing revenues, the less the amount it needs by way of additional mail pay; and the less the revenues the greater the additional mail pay. So the inclusion of a given amount in revenues lessens the mail pay by that amount, and the omission of an amount from revenues increases the needed mail pay. Such is our present problem.

The Board at first decided that the entire profit on the sale of Route 68 was "other revenue," and it included this amount as revenue in calculating the amount of mail pay needed by Western. The effect was to reduce the mail pay by that amount. Upon reconsideration the

⁵Of course the statute provides, in effect, for a minimum which is actual compensation for service performed. That payment is not in dispute here.

Board changed its position. It included the profit from the sale of tangibles as "other revenue" in its calculation, but it did not include the profit from the sale of intangibles. The effect was to reduce mail pay by the amount of the profit on the tangibles, but the profit on the intangibles was left out of the calculation entirely.

The Postmaster General is a party in interest by reason of the duties in respect to mail pay imposed upon him by the statute.⁶ He says the Board was in error in its treatment of the profit on the intangibles. Western says the Board was in error in its treatment of the profit on the tangibles. The Postmaster General would include in revenues the entire profit on the sale of the route and the equipment. Western would exclude the entire profit from revenues in the calculation.

We turn first to the problem of the profit on the tangibles. This was a gain derived from the sale of capital assets. As such it was "income" within the meaning which that term has had ever since *Doyle v. Mitchell Bros. Co.*⁷ But our problem is whether it was "revenue" within the meaning of this rate-making statute. We think the answer should be sought chiefly in the substantive meanings of the statutory provisions rather than in the semantics of the phrases.

The difficulty of the problem arises because this proceeding is to determine a rate of compensation for a past period. Ordinarily, of course, rates are fixed for the future. We think it clear that the profit from an isolated past sale of capital assets could not be included in a

⁶Sec. 406 of the Act, 52 Stat. 998 (1938), 49 U. S. C.-A. §486.

⁷247 U. S. 179, 62 L. Ed. 1054, 38 S. Ct. 467 (1918).

calculation of compensation to be paid in future years for carriage of the mail. It would not be anticipated revenue in the future period. With that proposition the Board agrees. In fixing the rate for the future it has considered as revenue only reasonably anticipated items.

Western bases its foremost argument upon the foregoing as a premise. It insists that the present proceeding is a rate-making proceeding and nothing else; that a rate-making proceeding must be, in contemplation of law, rate-making for the future—a prospective rate-making, since, it says, rate-making is inherently a prospective concept. The Board itself has several times so held. And, of course, that is a generally accepted view as to utility rates. There is great power in that argument.

But we are impressed by the practical aspects of the situation. In this instance the Board was in fact looking at a period which had passed. The actual facts as to revenues and expenses for that period were known. The actual need, or lack of it, of the carrier in that period was known. In saying that the Board was looking at a past period we are not departing from the rule in the *T. W. A.* case.⁸ The period began when the petition for the rate-making was filed, *i.e.*, May, 1944; as of that date the rate-making was prospective. When the Board got around to making its findings and decision the period 1944-1948 was past. It is to the latter actually that we refer.

At this point the two different considerations embodied in this statute must be noted. The statute provides for actual compensation for the service performed in carrying

⁸*T. W. A. v. Civil Aeronautics Board*, 336 U. S. 601, 93 L. Ed. 911, 69 S. Ct. 756 (1949).

the mail—a so-called service rate. This is the ordinary purpose of a utility rate. It involves reimbursement for expenses incurred in performing the service, return on the investment used in the service, and a reasonable profit on the transaction. This much is due whether the service is past or future. In the case at bar no dispute arises in respect to that phase of the matter.

But this statute adds to these ordinary features of a utility rate another consideration. It provides that the pay for carrying the mail shall be sufficient to meet the carrier's need. It describes that need as being for funds to perform the service of carrying the mail and also to maintain and develop air transportation. The problem under this provision of the statute is: How much does the carrier need? The answer depends upon (1) the gross, or total, need in dollars and (2) how much the carrier will have outside of mail pay.

In the ordinary case, where the rates are for the future, the revenue of the carrier must be anticipated. But where the pay is being computed for a past period may the Board accept as a fact that which it knows to be a fact, or must it ignore the known fact and compute the rate as though it were looking at the unknown future as of the date of the beginning of the period? The Board knew, and we all know, that Western had in this period this \$1,000,000, or thereabouts, in profit. That profit was derived from the disposition of assets acquired for or created by its operations under its certificate.

Let us suppose, as was the case in the basic findings here, that Western's total non-mail revenue was about \$33,000,000 and its total operating expenses were about \$36,000,000. How much does it need? How much does it

need if, in addition to the \$33,000,000, it also has a special profit of \$1,000,000? Does it actually need \$3,000,000, or does it actually need only \$2,000,000?

The gist of the answer lies in the fact that we are to determine "need." We are not determining merely adequate compensation for services rendered, in the ordinary public utility sense. To be sure, the payment is cast by the statute as a rate, and the process as a rate-making. But even so the Supreme Court held in the *West Ohio Gas* case⁹ that, when the period under consideration has passed, fair and reasonable rates should be ascertained from what is known and not from a *nunc pro tunc* estimate. In the case now before us the disputed basic consideration is a need, a need beyond the requirements of fair compensation for a service performed, not dependent upon the amount or the nature of the service rendered. *A fortiori*, from the *West Ohio Gas* case, the amount of need for a period which has passed must be ascertained in the light of known facts.

It seems to us that under this statute the Board, in fixing a rate of compensation for a past period, may view the facts as it knows the facts to be, that in determining "need" it is not compelled to ignore that which it knows. We conclude that in ascertaining Western's need for the period May, 1944, to December, 1948, the Board was permitted to take into consideration the fact that Western had this profit in that period from the sale of these assets.

We fully realize that our view of the statute will give rise to difficulties in respect to losses and also in respect

⁹*West Ohio Gas Co. v. Comm'n* (No. 2), 294 U. S. 79, 82, 79 L. Ed. 773, 55 S. Ct. 324 (1935).

to unusual or unanticipated earnings. The rule may make too much depend, from the standpoint of the carrier, upon tactical decisions whether and when to file petitions for rate-making. But we think such possibilities cannot negative statutory terms. Moreover other difficulties arise from any other rule. And, again, it seems to us that much of the anticipated difficulty can be prevented by expedition on the part of the Board, so that what is prospective in legal theory will be prospective in actual fact. If expeditious disposition of petitions does not meet the troubles arising from the rule, it is always possible that Congress may change the statutory provision. Our part is done when we conclude what Congress meant by the provision now before us.

We turn next to the treatment of the profit on the intangibles. The Board did not find, and it does not claim now, that Western itself needs the additional amount of mail pay which is shown when the profit on the sale of the intangibles in this transaction is omitted from "other revenue" in the computation. The claim of the Board is that it can allow Western to exclude this sum from stated revenues in order to encourage other carriers (not Western) to follow a given course of action. The Board said, in its opinion in the present case, that it wished to emphasize that the "decision not to include the net profit from the sale of intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers. In other words, we have decided not to offset this profit against the carrier's need because we are seeking in this way to spur the development of a self-sufficient air transport industry."

We recognize the force of the Board's description of the desirability of encouraging carriers to transfer routes and other property. But we cannot find in the statute any power conferred upon the Board to do so in fixing mail pay. We do not find any mail pay provision which is authority for the Board to provide incentives to the industry generally for the development of air transportation through the voluntary actions of carriers.

In the first place, the language of the statute sharply limits developmental allowances to the needs of the carrier under consideration. (1) The statute speaks of the "need" of the carrier. It does not speak of the desirability of allowances. It does not speak of purely bonus awards. (2) It speaks of "each" air carrier and compensation sufficient to enable "such air carrier" to develop. The statute is not cast in terms applicable to the general field of air transportation but to the situation in which each air carrier finds itself. (3) The statute provides that the mail pay shall be sufficient "to enable" the air carrier to maintain and continue development. This is a sharply limited expression. It does not extend to bonus awards which might be encouraging to the industry generally. Thus we think that, while the so-called "need" provision of the statute, above quoted, does provide for the payments of sums sufficient to enable the carrier under consideration to maintain and continue development of air transportation, such payments are restricted to the need of each individual carrier to maintain and continue a development program of its own.

In the second place, the Supreme Court held in the *T. W. A.* case, *supra*, that the mail pay provisions of this statute describe a rate-making authority, and the Court

said that the statutory language does not suggest that Congress intended to break with the traditions of public utility rate-making. Allowances designed as developmental incentives for the utility whose rates are being determined are quite common in public utility rate-making. But the award of bonus subsidies for the purpose of encouraging an industry generally to follow courses deemed desirable by the regulatory authority is a vast departure from rate-making. Mr. Justice Jackson made the distinction indisputably clear in his dissent in the *T. W. A.* case. He was of opinion that in these provisions of the statute Congress intended to subsidize the carriers and to underwrite their revenues. We think that the decision in the *T. W. A.* case as to the nature of the mail pay provisions leaves no room for bonus subsidies not connected with the particular carrier's own need. So the statute does not support the theory upon which the Board desires to go in this proceeding in respect to the profit from the intangibles.

We must conclude, therefore, on this point that the Board was in error in the theory upon which it excluded from the calculation the profit from the sales of the intangibles.

The parties dispute the Board's treatment of federal income tax liabilities in its computation of the mail pay. The tax liability upon an estimated basis as of the beginning of the period was some \$600,000. It developed that, due to carry-back losses and other provisions of the federal tax statutes. Western had little or no tax liability for this period. In its final orders on mail pay the Board acted upon the latter basis of fact. We think it was

correct in doing so. The preceding discussion is sufficient as a statement of our reasons.

Western also asserts that the Board erred in including as "other revenue" in the calculation of mail pay the profits derived from the operation of restaurants and slot machine concessions at its airports. We think the Board was clearly correct in this treatment. When the statute says "all other revenue" it must mean to include revenue derived from activities incidental to the operation of the airline. Whether it would also include revenue from activities unconnected with airplane operation is a question not before us and upon which we intimate no opinion.

Western asserts as reversible error the decision of the Board to fix in this proceeding the mail pay beginning in May, 1944. Western says that the consideration should have begun as of January 1, 1946. But the Board has power under the statute (Sec. 406(a)) to "make such rates effective from such date as it shall determine to be proper," and the Supreme Court held in the *T. W. A.* case that that clause empowered the Board to go back as far as the date of the filing of the petition. That is what the Board did in this case. Western filed its petition for redetermination of mail pay on May 1, 1944.

We add one further comment in regard to the expressions "offset," "deduction" and "recapture" used by the parties in describing the treatment of the profit from the sale of the assets if it be included in revenue. The phraseology would not be important if it did not embody

erroneous ideas. The need which this statute contemplates is a net figure; the extra amount which appears necessary over and above that which the carrier has. The process provided by the statute is for an affirmative ascertainment of that need. The need is not a gross figure from which offsets or deductions are made. Thus the passenger revenue etc., is not "offset" against or "deducted" from the need of the carrier. None of the earned revenue is recaptured. The bare, uncomplicated situation is that when the carrier has substantial revenues from non-mail sources the margin of its need for mail pay is less. In practical dollar effect, and perhaps in accounting entries, the treatment may be set up as a gross need with offsetting items, and so it takes on an appearance of recapture. But the legal contemplation of the statute is not that, and the use of the quoted terms leads to erroneous reasoning.

The necessity for reconsiderations, redeterminations and recalculations in the light of this opinion causes us to remand the matter to the Board. The remand is to enable the Board to determine, in the light of this opinion and pursuant to the statutory terms, the amount of compensation to be paid Western for the transportation of mail during the period here involved—May, 1944, to December, 1948.

Affirmed in part, reversed in part, and remanded.

BAZELON, *Circuit Judge*, concurring: I agree with the court's opinion and its comment that the rule we adopt in construing the statute "will give rise to difficulties in respect to losses and also in respect to unusual or unanticipated earnings"¹ but I am unable to agree that "much of the anticipated difficulty can be prevented by expedition on the part of the Board."² I think these difficulties or "other difficulties [which might] arise from any other rule"³ are inherent in the statute and will persist so long as there is no express differentiation therein between compensation for mail service and need payments to subsidize the development of air transportation. This is so because the absence of such a distinction, says the Supreme Court, requires the application of traditional principles of rate making.⁴ The effect of this is to make applicable to subsidy as well as compensation payments the familiar principle that "past excessive earnings belong to the [carrier] just as past losses must be borne by it."⁵ Therein lies the mischief. For that principle derives its validity from the premise that rates are calculated to allow for some financial risk on the part of the public utility.⁶ But since the very purpose of need or subsidy payments is to remove any vestige of risk, that principle has no place in fixing such non-rate payments.

¹Majority opinion, p. 8.

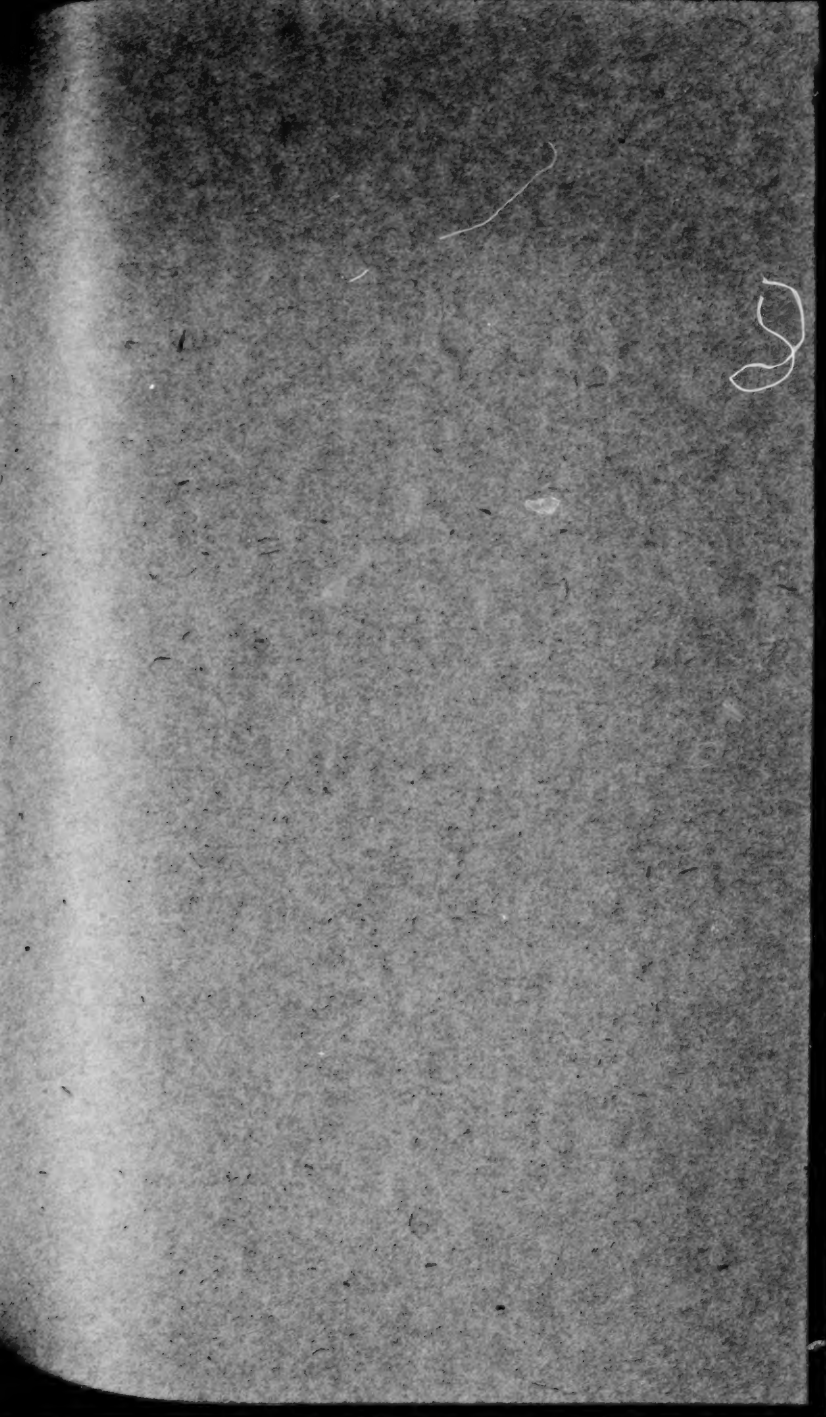
²*Ibid.*

³*Ibid.*

⁴*Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601, 605 (1949).

⁵*Washington Gas Light Co. v. Baker*, 88 U. S. App. D. C. 115, 125, 188 F. 2d 11, 21 (1950), *cert. denied*, 340 U. S. 952 (1951). And see my concurrence this day in *Summerfield, et al. v. Civil Aeronautics Board*, No. 11351.

⁶*Ibid.*, and cases cited in note 15 therein.



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APPENDIX B.

RATES FOR TRANSPORTATION OF MAIL

Board to Fix Rates

Sec. 406 [52 Stat. 998, 49 U. S. C. 486] (a) The Board is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith (including the transportation of mail by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same; and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft.

Rate-Making Elements

(b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers on classes

of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation⁷ of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

Statement of Postmaster General and Carrier

(c) Any petition for the fixing of fair and reasonable rates of compensation under this section shall include a statement of the rate the petitioner believes to be fair and reasonable. The Postmaster General shall introduce as part of the record in all proceedings under this section a comprehensive statement of all service to be required of

⁷So in original.

the air carrier and such other information in his possession as may be deemed by the Board to be material to the inquiry.

Weighing of Mail

(d) The Postmaster General may weigh the mail transported by aircraft and make such computations for statistical and administrative purposes as may be required in the interest of the mail service. The Postmaster General is authorized to employ such clerical and other assistance as may be required in connection with proceedings under this Act. If the Board shall determine that it is necessary or advisable, in order to carry out the provisions of this Act, to have additional and more frequent weighing of the mails, the Postmaster General, upon request of the Board, shall provide therefor in like manner, but such weighing need not be for continuous periods of more than thirty days.

Availability of Appropriations

(e) Except as otherwise provided in section 405(k), the unexpended balances of all appropriations for the transportation of mail by aircraft pursuant to contracts entered into under the Air Mail Act of 1934, as amended, and the unexpended balances of all appropriations available for the transportation of mail by aircraft in Alaska, shall be available, in addition to the purposes stated in such appropriations, for the payment of compensation by the Postmaster General, as provided in this Act for the

transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, between points in the continental United States or between points in Hawaii or in Alaska or between points in the continental United States and points in Canada within one hundred and fifty miles of the international boundary line. Except as otherwise provided in section 405(k), the unexpended balances of all appropriations for the transportation of mail by aircraft pursuant to contracts entered into under the Act of March 8, 1928, as amended, shall be available, in addition to the purposes stated in such appropriations, for payment to be made by the Postmaster General, as provided by this Act, in respect of the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, between points in the United States and points outside thereof, or between points in the continental United States and Territories or possessions of the United States, or between Territories or possessions of the United States.

Payments to Foreign Air Carriers

(f) If any case where air transportation is performed between the United States and any foreign country, both by aircraft owned or operated by one or more air carriers holding a certificate under this title and by aircraft owned or operated by one or more foreign air carriers, the Postmaster General shall not pay to or for the account of any such foreign air carrier a rate of compensation for transporting mail by aircraft between the

United States and such foreign country, which, in his opinion, will result (over such reasonable period as the Postmaster General may determine, taking account of exchange fluctuations and other factors) in such foreign air carrier receiving a higher rate of compensation for transporting such mail than such foreign country pays to air carriers for transporting its mail by aircraft between such foreign country and the United States, or receiving a higher rate of compensation for transporting such mail than a rate determined by the Postmaster General to be comparable to the rate such foreign country pays to air carriers for transporting its mail by aircraft between such foreign country and an intermediate country on the route of such air carrier between such foreign country and the United States.

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IN THE
Supreme Court of the United States

October Term, 1953
No. 225

WESTERN AIR LINES, INC.,

Petitioner,

vs.

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMERFIELD,
POSTMASTER GENERAL OF THE UNITED STATES, AND
THE UNITED STATES OF AMERICA, ON BEHALF OF THE
POSTMASTER GENERAL,

Respondents.

On Writ of Certiorari to the United States Court of Appeals
for the District of Columbia Circuit.

BRIEF FOR THE PETITIONER.

Opinions Below.

The opinion of the Court of Appeals¹ [R. 341-353] is not yet reported.²

The opinions and orders of the Board [R. 183-253, 258-281, 333-339] which were reviewed by the Court of Appeals are not yet reported.

¹The United States Court of Appeals for the District of Columbia Circuit will be referred to as the "Court of Appeals," Western Air Lines, Inc., as "Western," the Civil Aeronautics Board as the "Board," and the Civil Aeronautics Act as the "Act."

²The opinion of the Court of Appeals is included in this brief as Appendix A.

Jurisdictional Statement.

The judgment of the Court of Appeals was entered on May 4, 1953 [R. 354]. The petition for a writ of certiorari was filed on July 31, 1953, and granted on October 12, 1953 [R. 357]. The jurisdiction of this Court is invoked under Subsection 1254(1) of Title 28, U. S. Code, and Subsection 646(f) of Title 49, U. S. Code.

Questions Presented.

The Court of Appeals construed Subsections 406(a) and (b) of the Civil Aeronautics Act (52 Stat. 998; 49 U. S. Code, Sec. 486), relating to compensation for transporting air mail, as including within the term "all other revenue," which may be applied in the nature of an offset against mail compensation, Western's nonrecurring profit derived from the sale of a capital asset consisting of a route and the related flight equipment and the profit derived by Western from the operation of restaurants, canteens and slot machines. Likewise, the Court of Appeals construed the term "shall take into consideration, among other factors," as a mandatory direction that the Board apply and offset all of the "other revenue" derived by Western against Western's costs of operation in arriving at a fair and reasonable rate of compensation under Section 406, contrasted with the Board's construction that the term vests in it discretionary power.

The questions presented are:

1. Whether, in determining a fair and reasonable rate of compensation for the transportation of mail by aircraft under Section 406 of the Act for a past period under an application pending for seven years, the Board legally can offset against the mail compensation, as "other

revenue", any part of the nonrecurring profits derived from the extraordinary and nonanticipative sale of a capital asset consisting of an air route and the related flight equipment or any part of the profits derived from the operation of gambling machines in Nevada or the operation of restaurants and canteens?

2. Whether the term "shall take into consideration, among other factors," as used in Subsection 406(b) of the Act, makes it mandatory upon the Board, in fixing a fair and reasonable mail rate, to offset all of the "other revenue" of the carrier, as held by the Court of Appeals, or whether that language vests judicial discretion in the Board, as consistently held by the Board?

Statutes Involved.

Section 406 of the Civil Aeronautics Act is set forth in Appendix B of this brief. The pertinent provisions of Section 406, and the other sections of the Act which are indirectly involved, will be set forth at the places in the argument where they are mentioned.

Statement of the Case.

In response to a petition filed by Western on April 26, 1944 [R. 15-20], the Board in 1951 fixed the fair and reasonable final rate of compensation to be paid to Western for transporting the mail during the past period from May 1, 1944, through December 31, 1948, at \$3,917,361.00 [R. 338]. Both Western and the Postmaster General petitioned the Court of Appeals to review the orders of the Board. Western contended that the award was insufficient, whereas the Postmaster General contended that it was excessive. The Court of Appeals set aside the

orders of the Board in part and remanded the cases [R. 354].

The facts relevant to the area of dispute are simple. On September 15, 1947, after first obtaining the approval of the Board,³ Western sold one of its routes and the related equipment to United Air Lines for a book profit of \$1,095,102.00 [R. 196, 260, 336]. Also, during the period from May 1, 1944, through December 31, 1948, Western netted \$88,000.00 from the operation of slot machines in Nevada, under a concession obtained on open bids, and from the operation of restaurants and canteens [R. 153, 161, 192, 266]. Both the \$1,095,102.00 and the \$88,000.00 were considered by the Board to be "other revenue" within the meaning of Subsection 406(b) of the Act [R. 261, 267], but, in order to encourage voluntary route transfers, the Board took into account only \$648,102.00⁴ of the profit from the route sale in reaching the amount of mail compensation to be paid to Western [R. 262-265, 339].

The Court of Appeals agreed with the Board that the profits from the route sale and from the restaurants, canteens and slot machines were "other revenue," but ruled that the Board exceeded its authority under the Act when it excluded part of the profit from the route sale in its calculation of Western's final rate of mail compensation [R. 350].

³*United-Western, Acquisition of Air Carrier Property*. 8 C. A. B. 298 (1947).

⁴The Board's findings are that the sale transaction included both tangible and intangible elements of value. The amount of \$648,102.00 represents what the Board found to be the profit on the tangible property sold with the route. The remainder of \$447,000.00 is the part of the total profit attributed to the intangibles sold with the route [R. 279, 339].

Specification of Errors.

The Court of Appeals erred:

1. In holding that Western's profits from the route sale and from the operation of restaurants, conteens and slot machines were "other revenue" within the meaning of Subsection 406(b) of the Act.

2. In holding that the Board exceeded its authority under Section 406 of the Civil Aeronautics Act when it decided for public policy reasons to exclude part of the profit from the route sale in calculating Western's mail pay requirements.

Summary of Argument.

Subsection 406(a) of the Act is the enabling provision which delegates to the Board the power and duty of fixing fair and reasonable rates of compensation for the transportation of mail by aircraft. Subsection 406(b) sets forth guides to aid the Board in the exercise of this power and duty.

I.

In fixing the fair and reasonable rate of mail compensation, the Board is required to take into consideration "all other revenue of the carrier," and, if it elects so to do,⁵ may offset the other revenue, in whole or in part, against the carrier's operating costs, which has the end result of reducing the mail compensation to the extent of the other revenue which is applied as an offset.

⁵The Court of Appeals held that application of the "other revenue" in the nature of an offset against the mail compensation was not a discretionary right, but mandatory, which constitutes the second question involved on this review.

The Postmaster General urged below that "all other revenue" means all other income regardless of source. The Board, with which the Court of Appeals apparently concurred, took the position that "all other revenue" does not mean all income regardless of source, but does include income of an air carrier from activities related to air carrier functions. Western consistently has urged that the term can only mean revenue derived by a carrier from transporting persons and property.

The Congress intended in Section 406 to provide for the customary pattern of fixing rates prospectively. (*Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949).) Accordingly, "all other revenue" as used in Subsection 406(b) can only embrace revenue which is subject to reasonable anticipation.

Under Subsection 404(a) (49 U. S. Code, Sec. 484) all air carriers, except the few with certificates limited to the transportation of mail alone or the transportation of property alone, are required to carry passengers and property. The revenue which an air carrier will derive from transporting passengers and property is susceptible of forecast by the Board. The profit, if any, from unusual and non-recurring sales of capital assets, and the profits, if any, from operating gambling concessions which may be discontinued at any time voluntarily or by operation of law or from operating restaurants which may be stopped or started at the will of the carrier are not subject to forecast. The word "revenue" as used in Subsection 406(b)

cannot have one meaning for the future and another meaning for the past.

The term "all other revenue" connotes a gross amount, as distinguished from a net profit. Since the mail compensation under the Act contemplates that an air carrier's operating costs or "need" shall be met through mail compensation, it is proper that the gross income generated by those operating costs, which can consist only of revenue from carrying passengers and property, be applied in the nature of a reduction of mail compensation. Net profits from a collateral activity, even though related to air carrier functions, do not meet this measure. This postulate is sealed by the fact that the Act does not contemplate recoupment, by means of mail compensation, of losses from either related or unrelated activities.

The whole thread of the Act contemplates that the owners, whether shareholders or individuals, of an air carrier will supply and replace the capital assets, and that the Government, by means of air mail compensation, will pay (i) the cost of transporting the mail and (ii) the cost of maintaining complete air transportation service consisting of additional facilities for carrying passengers and property, which latter cost is offset by the revenue derived from that source. If the revenue from the second phase of the service is inadequate to meet the cost, it is the statutory obligation of the Government to meet it.

II.

The Congress directed the Board to "take into consideration, among other factors," the carrier's "need" for compensation sufficient to enable it (i) to transport the mail and (ii) together with "all other revenue of the air carrier" to maintain and continue the development of air transportation. In addition, the Congress directed the Board to take into consideration the condition that air carriers authorized to carry mail are required to provide necessary and adequate facilities and service for the transportation of mail, as well as the standards prescribed by law respecting the character and quality of air service. The "other factors" which the Board may consider are not named, but, of necessity, vary in importance with the facts of each case.

The Court of Appeals accepted the contention of the Postmaster General that after taking into consideration the guides enumerated, the Board was under a mandate to act affirmatively. The Board, with which Western fully and firmly concurs, took the position that after considering these guides it has the discretionary power to act affirmatively or negatively as the public interest dictates.

These guides imply that the process of fixing fair and reasonable mail rates must be left to the informed judgment and discretion of the Board. The Board is not fettered to the factors set forth in the statute, but enjoys a discretion commensurate with the broad purposes of

the Act. (*New York v. United States*, 331 U. S. 284 (1947); *Secretary of Agriculture v. Central Roig Refining Co.*, 338 U. S. 604 (1950).)

In the performance of its duties—including the duty to fix mail rates—Section 2 of the Act requires the Board to consider, among other things, the encouragement and development of an air transportation system properly adapted to the present and future needs of the nation.

The Board here sought to induce voluntary route transfers by establishing and implementing a rate-making policy under which part of the profit from voluntary transfers—assuming, over Western's denial, such profit to be "revenue"—would be excluded in fixing mail rates under Section 406. The Court of Appeals conceded the desirability of encouraging voluntary action by carriers to sell routes that could be operated by other carriers to better advantage, but failed to find in Section 406 any authority for declining to offset the profit from any such sale against the selling carrier's mail compensation under Section 406, even though the purpose be to encourage other carriers to take similar action.

Had the Congress intended to impress a mandate on the Board the discretionary term "shall take into consideration, among other factors," would not have been employed. Mandatory words of unequivocal tenor were near at hand.

ARGUMENT.

I.

The "Other Revenue of an Air Carrier" Which May (Not Must) Be Applied in the Nature of an Offset Against the Fair and Reasonable Rate of Compensation for Carrying the Mail Is Limited to Revenue Derived From Carrying Passengers and Air Express.

- A. The Theory of the Court of Appeals and the Board That "All Other Revenue" Means All Income From Activities Related to Air Carrier Functions and the Theory of the Postmaster General That "All Other Revenue" Means All Income, Regardless of the Source, Are Illegal and Illogical.

In fixing fair and reasonable rates of compensation for the transportation of mail by aircraft under Subsection 406(a), the Board is required under Subsection 406(b) to take into consideration, among other factors,

" . . . the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, *together with all other revenue of the air carrier*, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."⁶

Western holds to the view that the word "revenue", as used in Subsection 406(b), has a limited application and

⁶Emphasis in quoted material added throughout unless otherwise noted.

includes only the gross moneys received by an air carrier for the transportation of persons and property.

At the outset of its opinion the Court of Appeals properly stated the issue raised by the italicized language of the statute in this fashion:

“ . . . Now, obviously, in this calculation the greater the amount of the carrier's existing revenues, the less the amount it needs by way of additional mail pay; and the less the revenues the greater the additional mail pay. So the inclusion of a given amount in revenues lessens the mail pay by that amount, and the omission of an amount from revenues increases the needed pay. Such is our present problem.” [R. 344.]

But the Court of Appeals failed to meet the problem head-on, not once revealing its interpretation of the term “revenue.” The opinion could be read as construing “revenue” to mean “income” from whatever source.⁷ However, it is probable that the Court of Appeals intended to adopt the Board's theory.

The Board has conceded that the term “revenue” has limitations and does not include all income, regardless of source, but the statutory basis for the Board's interpreta-

⁷The Court of Appeals stated:

“The Board knew, and we all know, that Western had in this period this \$1,000,000, or thereabouts, in profit.

* * * * *

“It seems to us that under this statute the Board, in fixing a rate of compensation for a past period, may view the facts as it knows the facts to be, that in determining ‘need’ it is not compelled to ignore that which it knows.” [R. 347, 348.]

tion has never been stated.⁸ It draws a blurred line as to what is or is not "revenue" under Subsection 406(b) in relation to the character of the activities giving rise to income. Thus, the Board interprets "revenue" to mean all income of an air carrier from activities related to air carrier functions,⁹ reasoning in this case that the sale of a route and the operation of a slot machine concession and restaurants and canteens were activities related to air carrier functions.¹⁰ Even if Western's interpretation of the statute were too limited, the term "revenue" still will not bear a construction which would include these special items of income.

The Postmaster General argues that "revenue" is synonymous with "income" and that all income of an air

⁸In *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C. A. B. 267 (1947), at page 290, the Board declared:

"'All other revenue' within the meaning of section 406(b) could hardly have been intended to include revenues from every possible source . . ."

⁹In its opinion here of November 24, 1950, the Board stated:

"Where the activity from which the income arose is related to the air carrier functions, such income should be considered as 'other revenue.'" [R. 193.]

¹⁰Many of the Board's decisions as to what is and what is not "revenue" are cited in *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C. A. B. 267 (1947), at pages 289 to 290. The Board has not considered as "other revenue" under Subsection 406(b) such items of income as net gain from the operation of pilot training schools, the manufacture and sale of pick-up devices, crop-dusting operations, military charter flights and military contracts. In the *Pan American* case the Board held that the profit realized by Pan American from the sale of stock in a foreign air transportation company was not "other revenue." On the other hand, it has included in "other revenue" such items of income as cash discounts earned and interest income from investments. (*Continental Air Lines, Mail Rates*, 8 C. A. B. 825 (1947); *Delta Air Lines, Mail Rates*, 9 C. A. B. 645 (1948).)

carrier, regardless of source, must be included in the calculation of "need" under the statute.¹¹

It is obvious that the meaning of "revenue" was not resolved below. One of the three theories—Western's, the Board's or the Postmaster General's—is correct. No other construction of the statute can be conceived. And, if this Court's imprimatur be placed on the interpretation reached by the Board, the question of the proper application of that theory still remains. Otherwise, the argument would be left open that all activities of an air carrier are related to air carrier functions simply because the actor is an air carrier. This is impressively illustrated here. Western's slot machine concession rights in Las Vegas, Nevada, were held under a separate lease which was awarded following a public invitation to bid.¹² If the income Western derived from slot machines be revenue, then *any* income derived by an air carrier from *any* possible source is revenue, and the Board's theory in its application does not differ from the Postmaster General's.

This leads to an analysis of the correct meaning of the expression "all other revenue of the air carrier." If

¹¹On page 21 of the Postmaster General's Brief to the Court of Appeals, this statement is made:

"Moreover, it is evident that the carrier's actual need can be determined only by a comparison of its actual income *from all sources*, with the amount of income determined by the Board to be sufficient to enable the carrier to perform its transportation functions properly and to receive a fair return on its investment."

¹²Exhibit WX-3, R. 161; Exhibit WX-4, R. 161; Exhibit W-12, R. 153.

“revenue” was intended by the Congress to have a restricted meaning, and the Board concedes this, the Board is restrained to the consideration of only those items of income which fall within the meaning.

B. The Word “Revenue” Has a Restricted Meaning and Was Used in a Restricted Sense in Subsection 406(b).

As stated by Mr. Justice Sutherland in *Puerto Rico v. Shell Co.*, 302 U. S. 253 (1937):

“Words generally have different shades of meaning, and are to be construed if reasonably possible to effectuate the intent of the lawmakers; and this meaning in particular instances is to be arrived at not only by a consideration of the words themselves, but by considering as well, the context, the purposes of the law, and the circumstances under which the words were employed.” (P. 258.)

“Revenue” is an equivocal word, the meaning of which depends upon the context in which it is used.¹³ For instance revenue is used to denote public income, as from taxes. And in the case of common carriers, it most often refers to the principal classes of gross operating income which a carrier realizes.

“Revenue” is used twice in the Act. The second time is in Subsection 1002(e) (49 U. S. Code, Sec. 642), which reads in part:

“In exercising and performing its powers and duties with respect to the determination of rates for

¹³In *Bates v. Porter*, 74 Cal. 224, 15 Pac. 732 (1887), the Supreme Court of California stated:

“The word ‘revenue’ is used in many senses. It is, like thousands of words in our language, ambiguous in meaning, the significance of which can only be determined by the words with which it is connected.” (P. 240.)

the *carriage of persons or property*, the Board shall take into consideration, among other factors—

* * * * *

“(5) The need of each air carrier for *revenue* sufficient to enable such air carrier, under honest, economical, and efficient management, to provide adequate and efficient air carrier service.”

The word “revenue” in Subsection 1002(e)(5) means revenue accruing from the rates charged for the carriage of persons and property. It cannot possibly mean anything else. Subsection 406(b) requires the Board to consider the “other revenue” of the carrier. Without question the Congress intended to include within this expression the revenue referred to in Subsection 1002(e)(5).

It is noteworthy that the word “other” is used in context with “revenue” in Subsection 406(b), giving to mail compensation the same attribute of being “revenue” that income from the transportation of persons and property has under Subsection 1002(e)(5). Thus, the principal classes of gross operating income of air carriers—from the carriage of persons, property and mail—are tied to the word “revenue”. No other form of income is provided for or referred to in the Act.

It also should be noted that Subsection 406(b) refers to “honest, economical, and efficient management.” This test, common to most if not all rate-making statutes, requires the Board to screen the reported operating costs of each air carrier and then compare the adjusted costs of operation to what the carrier has received in the way of revenue. The obvious implication is that “revenue” is a gross figure, not the net profit after accounting for the

expenses of running slot machines or the excess of the sales price over the cost of a capital asset.

If "revenue" include amounts of net profit from collateral activities, related or unrelated to air transportation, then the Board would be remiss in failing to scrutinize the costs of activities giving rise to the special profits to determine if management acted honestly, economically and efficiently, in connection with those activities. It is certain that the Congress had no intention of burdening the Board members with being experts not only in the field of air transportation but experts as well in every extracurricular field in which an air carrier conceivably might engage, the range of which is bounded only by general corporate laws.

The reference in Subsection 406(b) to revenue "of the air carrier" is of more than passing significance. An air carrier under Subsection 1(2) of the Act (49 U. S. Code, Sec. 401) is "any citizen of the United States who undertakes . . . to engage in air transportation." Accordingly, in using the words "revenue of the air carrier" in Subsection 406(b) the Congress must have intended to mean the revenue which the air carrier would derive from being engaged in air transportation. Air transportation under Subsection 1(10) of the Act includes interstate air transportation, which in turn under Subsection 1(21) means "the carriage by aircraft of *persons* or *property* as a common carrier for compensation or hire or the carriage of *mail* by aircraft" Thus, the Congress could have had in mind in Subsection 406(b) only the

revenue derived from the carriage of persons or property, as the compensation resulting from the carriage of mail is the principal subject of Section 406.

The clear design is that "other revenue" in Subsection 406(b) pertains solely to the "revenue" described in Subsection 1002(e), arising from the rates charged by air carriers for transporting persons and property. It is only such receipts that the Board legally may consider in determining "need" under the statute.¹⁴

Had the Congress intended "revenue" in Subsection 406(b) to have a meaning synonymous with "income" or a more expansive meaning than revenue from the carriage of persons and property, it would have used language appropriate to its intent.¹⁵

¹⁴In *Atlantic Coast Line R. Co. v. Public Service Commission*, 77 Fed. Supp. 675 (1948), the United States District Court for the Eastern District of South Carolina stated:

"The railroad's income *from sources other than its own railroad operations* should obviously not be taken into account in considering the confiscatory effect of the Commission's actions." (P. 683.)

¹⁵E. g., in the Air Mail Act of 1934 (48 Stat. 933) these expressions were used: "*all forms of gross income*" (Subsec. 6(b)); "*revenues and profits from all sources*" (Subsec. 6(e)). And, in Subsection 606(5) of the Merchant Marine Act of 1936 (49 Stat. 2004), this expression was used: "*net profit . . . (without regard to capital gains and capital losses)*" . . .

In *Air Mail Compensation*, 206 I. C. C. 675 (1935), the Interstate Commerce Commission held that the expression "revenues and profits from all sources"—a much broader category than "all other revenue"—did not extend to off-line passenger and express operations, declaring:

"Revenues from 'all sources,' if extended to off-line passenger and express operation, are broad enough to include revenues from sources entirely unrelated to air transportation. No matter how sound such ventures may appear, nor how profitable or unprofitable they may be, they cannot be regarded as within the contemplation of the Act." (P. 697.)

C. The Congress Did Not Intend in Section 406 to Depart From the Customary Pattern of Fixing Rates Prospectively, Thus Limiting the Meaning of "Revenue" to Passenger and Express Tariffs.

Even if use of the word "revenue" of itself is not deemed sufficient to invalidate the Board's action, affirmed by the Court of Appeals, the purposes of the Act clearly place a restricted meaning on the word.

The manifest intent of the Congress in Section 406 is that rates of compensation for the transportation of mail by aircraft will be fixed prospectively. This Court so held in *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949). And the Board at all times since its creation has acted on this premise. Only where lack of expedition in a mail rate proceeding has occurred, as in this case, has the Board been confronted with fixing a "retroactive" rate. Hence, the word "revenue" could have been intended by the Congress to include only the income of an air carrier which is subject to reasonable anticipation.

Revenue derived from the transportation of persons and property is the only type of income which can be forecast by the Board with any certainty and within range of fairness, since all certificated air carriers are required to carry passengers and property in addition to mail (Subsec. 404(a) of the Act), except those carriers that have certificates limiting their operation to the transportation of mail alone or property alone.

Income which may be derived from collateral sources, such as the operation of slot machines, restaurants or canteens, cannot be predicted by the Board with any certainty or any fairness. One very simple reason for this is that no airline is required by its certificate to operate slot machines or restaurants or canteens and is at liberty, where state law permits, to commence or discontinue such activities at will. Another reason is that the Board is not expert in the field of slot machines, restaurants and canteens, as it is in the field of air transportation.

By the same token, a nonrecurring, sporadic capital gain (or loss) resulting from the sale of a vacant lot purchased at one time, out of funds made available by the shareholders, in anticipation of the construction of a ticket office or the sale of antiquated equipment or the sale of a route, cannot possibly be anticipated in advance. If Western had not had an application to fix its mail rate pending at the time it sold its Los Angeles-Denver route and the related equipment to United Air Lines, the principal point of issue dollarwise on this review would not have been an issue below. The meaning of "revenue" is not enlarged or reduced simply on the basis of the point of time at which a rate proceeding is commenced. The word "revenue," as used in Subsections 406(b) and 1002(e), has a definite meaning, whatever this Court decides it to be, and does not change its color because the Board is considering a past as opposed to a future rate period.

D. The Limitation of "Revenue" to Passenger and Express Tariffs Is Confirmed by the Fact That the Board Has Control Over Passenger and Express Rates, But No Control Over Income Derived by a Carrier From Collateral or Incidental Activities.

Another significant factor which exposes the fallacy of the interpretation below of "all other revenue" is that under the Act the Board has control over and power to prescribe the revenue of air carriers *only* with reference to the three principal sources of air carrier income—passengers, property and mail. Section 1002 gives the Board the power to determine and prescribe the rates which an air carrier may charge for transporting passengers and property. Section 406 empowers the Board to determine and fix rates of compensation for transporting the mail. The Board has no power to determine the prices an air carrier shall charge or the amount of income an air carrier shall receive in connection with incidental or collateral activities—operating restaurants or slot machine concessions. The Congress realized the significance of this and deliberately chose the word "revenue" for use in Subsections 406(b) and 1002(e).

Considering that the Board has control over the revenues derived from transporting passengers and property—the cost of which, less the resulting revenues, the Government has underwritten under the Act—and thus has the power to see to it that those revenues are productive of the maximum amount possible, the Congress wisely and rightly provided that the Board should consider those revenues in fixing a fair and reasonable rate of compensation for transporting the mail.

But under light of the fact that the shareholders who furnish the capital must bear the burden of losses from the sale of capital assets, including routes, and from incidental or collateral activities, with a corollary right to the profits, plus the fact that the Board does not have the power to determine the prices that an air carrier shall charge or receive in connection with sales of capital assets or incidental or collateral activities, the Congress, again wisely and rightly, by using the restricted word "revenue," excluded these types of income from the air carrier receipts which may (not must) be applied as an offset against mail compensation.

E. Judicial Enlargement of the Meaning of "Revenue" Would Shift to Western's Shareholders the Burden Imposed Upon the Government by Section 406.

If this Court were to approve the interpretation placed upon the word "revenue" in Subsection 406(b) by the Court of Appeals, it would mean that Western's shareholders would be required to pay a part of the cost of the development of air transportation service which the Government is bound by statute to pay if the revenue from that service be insufficient to meet the cost.

It is common knowledge that prior to 1938 the air transportation industry was in a competitive and economic quagmire and that the Civil Aeronautics Act of 1938 was enacted by the Congress to inject competitive and financial stability into the industry by requiring certificates of public convenience and necessity and by underwriting the cost of providing complete air transportation service through mail compensation. The Federal Government thus was put to the task of developing a first-rate and

self-sufficient air transportation system not alone to provide speedy and efficient air mail service but, more important, a system which would give to this country the commercial air service required to meet the ever-increasing demands of the foreign and domestic commerce of the nation and the national defense. To accomplish these purposes, the Government was made responsible for insuring that private industry, which was to furnish the property and equipment and the necessary capital, would realize a reasonable profit on its investment, assuming an honest, economical and efficient management.

The goal was to build a system of air carriers which, in time, would be made self-sufficient by payments directly from the users of air service, including the Government. But, until the revenues from transporting passengers and property, together with revenues for carrying mail, proved sufficient to meet the cost of air service plus a reasonable return, the public, through its national treasury, was to underwrite the difference.

It is self-evident that the scheme adopted by the Congress was intended to place the *ultimate* burden of the cost of air service on the people who use it, with the *interim* burden, pending attainment of self-sufficiency by the industry, on the public at large.

The cost of transporting persons, property and mail is an ascertainable quantity. It does not include and is not affected by the cost of running a restaurant or operating slot machines, nor by the cost price of capital assets which are sold. Management's only responsibility in such incidental activities is to its shareholders—the Board having no control here—and it is only proper that the shareholders who furnished the capital, not the Govern-

ment, should benefit from the profits and bear the losses from those activities.¹⁶

To require that the profit from the sale of a route or any other capital asset or the profit from running a restaurant or operating slot machines be applied to take up part of the cost of air service which the Congress has committed the Government to buy, if the traveling public does not, would mean that Western's owners, its shareholders, would be bearing the Government's statutory burden.

That result would be doubly intolerable unless the public which would enjoy the benefit of such profits were required to bear any losses from the same activities, although not a necessary part of air transportation. It is inconceivable that the Congress intended to burden mail rates with losses from the incidental activities in which a carrier might engage.

The only intelligible interpretation of Subsection 406(b) is that the Congress intended "all other revenue" to be limited to the gross returns of an air carrier from transporting persons and property.

¹⁶It would appear that in at least one of its fairly recent decisions the Board was not unsympathetic to this philosophy, as indicated by the following statement taken from *Pan American Airways, Inc., Transatlantic Mail Rates*, 8 C. A. B. 267 at 290 (1947):

"'All other revenue' within the meaning of section 406(b) could hardly have been intended to include revenue from every possible source unless the Act had intended that air carriers should not be permitted, at least so long as they might receive subsidy mail pay, to engage or invest in non-air-carrier activities. Yet there is no indication in the Act that such was its intent. Clearly, in determining need we could not consider net losses sustained by a carrier in non-air-carrier activities. To do so would result in Government subsidization of such activities through mail payments without any statutory authority therefor. Yet if we were to consider the profits from such activities to reduce need, we would place the carrier in the position of standing all losses from such activities but reaping no benefits from the profits so long as it remained on a subsidy basis."

II.

The Term "Shall Take Into Consideration, Among Other Factors," as Used in Section 406 Is Not Mandatory in the Sense That the Board Must Give Controlling Significance to Any of the Rate-making Elements, as Erroneously Held by the Court of Appeals, but Vests Judicial Discretion in the Board, as Correctly Held by the Board.

- A. Had the Congress Intended to Require the Board to Give Controlling Significance to Any of the Rate-making Elements Specified, Mandatory, Not Discretionary, Words Would Have Been Used.

Section 406 requires that the Board fix fair and reasonable rates of compensation for the transportation of mail by aircraft and directs that, in determining the rate in each case, the Board "take into consideration" certain enumerated rate-making elements "among other factors."

The holding of the Court of Appeals was that mail payments to air carriers under Section 406 are restricted to the "need" of individual carriers for compensation—which is only one of the rate-making elements set forth in the statute—and may not be employed for the purpose of encouraging the industry generally, including the air carrier directly affected, to follow a course of action deemed by the Board to be in the public interest but which the Board is powerless to require of air carriers [R. 349, 350].

Parenthetically, it might be noted here that the word "need" in Subsection 406(b) applies equally and alike to compensation both (i) for the transportation of mail, and (ii) together with all other revenue, for maintaining and continuing the development of air transportation. None-

theless, the Postmaster General, the Board and the Court of Appeals in unison concede (and Western agrees) that all carriers, the rich as well as the poor, are entitled as the bare minimum to a so-called compensatory mail rate, regardless of the source, extent or lack of other income. Thus, in arguing that mail compensation for carrying the mail alone is just that—compensation—but that compensation for maintaining and continuing the development of air transportation is sheer subsidy or an outright gratuity, the debaters tint the word “need” with two clashing colors. Stated another way, as applied to the transportation of mail the proponents proclaim that “need” in effect means cost plus a fair profit, but when the same word in the same sentence is applied to the maintenance and continuation of air transportation it involves something entirely different—actual economic need. One word in one sentence referring to two clauses cannot be given two entirely different meanings.

Consistently the Board has interpreted “take into consideration” to mean what simple semantics would have it mean, the discretionary right of doing what good judgment dictates in accordance with the circumstances prevailing in each situation under consideration. The Board always has thought, and rightly so, that the only mandate which it was required to meet was to *consider* the guides set out by the Congress and then act affirmatively or negatively in response to its judicial discretion.

Had the Congress intended to bind the Board as to the weight or significance to be given to the factors named in Subsection 406(b), it would have been simple to use language that could not have been misconstrued, assuming there be justification for the misconstruction placed upon

the language of the statute by the Court of Appeals and the Postmaster General.¹⁷ Moreover, had the Congress intended that "take into consideration" would require positive action, beyond the act of considering, it is not likely that the term would be followed by the clause "among other factors," without identifying those other factors.

B. It Was the Avowed Intent of the Congress to Cloak the Board With Broad Judicial Discretion Concerning the Action to Be Taken With Respect to the Various Rate-making Elements.

The words of Subsection 406(b), set up by the Congress to guide the Board in reaching fair and reasonable rates of mail compensation, do not inhibit the Board in the responsible exercise of its broad rate-making power, provided the Board acts with fairness and in relation to the attainment of the legislative purposes.

The mandate of the statute is that the Board "take into consideration" the named factors "among other factors." This means that the Board is required to give such weight or significance to the appropriate rate-making elements as the circumstances merit. It means no more than that. The choice is left to the informed judgment of the Board, and, while the Board must consider the

¹⁷In his Petition to Reconsider before the Board dated July 27, 1951 [R. 282-289], the Postmaster General stated:

" . . . in the consideration of whether the development of air transportation requires a subsidy to a particular carrier in addition to compensation for services rendered, as directed by the same action, the Board has *no discretion* under such section but must take into account all other revenue of such carrier obtained from all sources." [R. 284.]

factors specified by the Congress, it need not act wholly or partially in response to any of them.¹⁸

Rate-making is the function of experts. Courts may not upset rate determinations simply because they would have appraised differently the value or weight of the factors in the rate-making process. As stated by Mr. Justice Douglas in *New York v. United States*, 331 U. S. 284 (1947), regarding Section 15(a)(2) of the Interstate Commerce Act:

"The balancing and weighing of these interests is a delicate task . . . There may be differences of opinion concerning the weight to be given those factors . . . But their significance is for the Commission to determine; and, though we had doubts, we would usurp the administrative function of the Commission if we overruled it and substituted our own appraisal of these factors." (Pp. 347, 349.)

¹⁸In *United States v. Interstate Commerce Commission*, 88 F. 2d 780 (1937), certiorari denied, 300 U. S. 684 (1937), the United States Court of Appeals for the District of Columbia construed the words "due consideration," appearing in Section 15(a)(2) of the Interstate Commerce Act, in this manner:

"The mandate of the act . . . is that the Commission shall give 'due consideration.' To give due consideration to a particular factor *necessarily means to give such weight or significance to it as under the circumstances it seems to merit*, and this, of course, involves discretion; and, as has been said many times, *judicial discretion*." (P. 783.)

In the early case of *Babb v. Carver*, 7 Wis. 124 (1859), the Supreme Court of Wisconsin had before it a statute which required the Town Supervisors to give notice of the time and place at which they would meet to decide an application to lay out a highway. The notice which was issued was that they would meet at a certain time and place to "take into consideration" a particular application. The court held that the notice was defective stating:

"The notice is not that they would there decide upon the petition, but would take it into consideration, or deliberate upon it. This they might do, without even deciding upon the application." (P. 126.)

In *Baltimore & Ohio Railroad Co. v. United States*, 345 U. S. 146 (1953), Mr. Justice Black had this to say:

"This mere sample of factors that have to be considered in rate cases demonstrates the *absolute necessity for considerable flexibility in rate-making* . . . Commission power to adjust rates to meet public needs is implicit in the congressional plan for a nationally integrated railroad system." (P. 152.)

The Court of Appeals did not presume to question the significance of what the Board sought to accomplish in this case. However, it blindly failed to find any authority in the statute for providing industry incentives through mail pay. Instead, the Court found that Section 406 and the decision of this Court in *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949), leave no room for mail compensation not connected with the particular carrier's own "need."

The Court of Appeals misread Subsection 406(b). The "need" of an air carrier for mail compensation sufficient (i) to enable it to provide mail service and (ii) to maintain and continue the development of air transportation is only one of the factors which the Board is directed to consider, "among other factors." In addition, the Board is required to give consideration to the standards prescribed respecting the character and quality of air service and the condition that air carriers authorized to carry mail must provide necessary and adequate facilities and service for the transportation of mail. Beyond these factors are the "other factors" which are not named

but which the Board may consider. This is a framework of broad discretion, not ironclad compulsion.¹⁹

Peculiarly applicable to the point under discussion are these statements of Mr. Justice Frankfurter in *Secretary of Agriculture v. Central Roig Refining Co.*, 338 U. S. 504 (1950):

"By way of guiding the Secretary in formulating a fair distribution of individual allotments, *Congress directed him to exercise his discretion 'by taking into consideration' three factors: past marketings, ability to market, and processings to which proportionate*

¹⁹In *United States v. Interstate Commerce Commission*, 88 F. 2d 780 (1937), certiorari denied, 300 U. S. 684 (1937), the United States Court of Appeals for the District of Columbia made these statements:

"Putting aside all questions of relative importance of the various elements of rate making—because the controlling facts in each case necessarily vary—there can be no doubt that in prescribing reasonable rates the Commission is required to take into consideration, *among other factors*, first, the effect of the rate on the movement of traffic; second, public need of adequate low-cost service; third, the carrier's need of sufficient revenue to enable it to give such service. This, we think, is the clear mandate of the statute. *But the weight to be given to these several factors is left to the discretion of the Commission, as is also the weight to be given the other and unnamed factors which of necessity vary in substance according to the facts.*" (P. 782, first italics included.)

In *Chicago B. & Q. R. Co. v. United States*, 60 Fed. Supp. 580 (1945), the United States District Court for the Eastern District of Kentucky declared:

"Congress has not prescribed the 'other factors' to be considered by the Commission in the exercise of its power to fix just and reasonable rates. *The determination of the issue of fact in respect to reasonableness as well as the choice of the standard upon which the determination is to be made in each particular case, is left to the informed judgment of the Commission . . .*" (P. 585.)

shares pertained. *Plainly these are not mechanical or self-defining standards. They in turn imply wide areas of judgment and therefore of discretion. The fact that the Secretary's judgment is finally expressed arithmetically gives an illusory definiteness to the process of reaching it. Moreover, he is under a duty merely to take 'into consideration' the particularized factors. The Secretary cannot be heedless of these factors in the sense, for instance, of refusing to hear relevant evidence bearing on them. But Congress did not think it was feasible to bind the Secretary as to the part his 'consideration' of these three factors should play in his final judgment—what weight each should be given, or whether in a particular situation all three factors must play a quantitative share in his computation.*" (Pp. 611-612.)

In the case here the Board's judgment was expressed in an award of money. The Board considered Western's costs or "need," the quality and character of the service required of Western and the condition that Western was required to provide necessary and adequate facilities and service for the transportation of mail. It also considered the important public interest in voluntary route transfers. The resultant award was a composite of these elements, and not the result of considering any one of them alone. The fact that the Board reached the amount of the award by eventually excluding from its computations part of Western's profit from the sale of a route is immaterial. This was the Board's measure of the incentive required to induce voluntary realignment of

the nation's route pattern. If the Board has the power to provide the incentive—and it has—the Board's discretion to fix the amount of the incentive cannot be gainsaid.²⁰

C. The Expression "Among Other Factors" in Subsection 406(b) Authorizes the Board to Consider Factors Not Specified in the Subsection and Demonstrates the Irrefragable Intent of the Congress That the Board Should Have Broad Judicial Discretion in Fixing Air-mail Rates.

The Board rested its holding in part upon the determination that there was a public need for readjustment of the air route pattern through route transfers between air carriers, in order to correct undesirable and uneconomical route structures existing in the air transportation system of this country. Recognizing that it was without power to compel air carriers to transfer routes or to merge, the Board fixed upon a policy which would preserve at least a part of the profit incentive to voluntary route adjustments.

The Court of Appeals did not deny the existence of a public need for voluntary route transfers. What the Court of Appeals denied was the Board's statutory power

²⁰The case of *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949), did not concern the elements which the Board must or may consider, or the part such elements must or may play, in the rate-making process. The issue in that case went to the meaning of the "make effective" clause in Subsection 406(a). This Court's construction of the statute in that regard in no way predetermines this case, as suggested by the Court of Appeals.

to encourage carriers, including Western, to transfer routes, by establishing and implementing a policy affecting mail rates.

In fixing rates, as well as in the exercise of its other powers and duties under the Act, the Board is required under Section 2 (52 Stat. 980; 49 U. S. Code, Sec. 402)²¹ to consider, and within its discretion may act to bring about, among other things, the encouragement and development of an air-transportation system properly adapted to the needs of the nation, the regulation of air transportation in such a manner as to foster sound economic conditions and the promotion of adequate, econom-

²¹Section 2 reads:

"In the exercise and performance of its powers and duties under this chapter, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

"(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

"(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers;

"(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

"(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

"(e) The regulation of air commerce in such manner as to best promote its development and safety; and

"(f) The encouragement and development of civil aeronautics."

ical and efficient service by air carriers at reasonable charges.

The importance of mail rates as a device to accomplish the policies set forth in Section 2 was recognized by this Court in the *Transcontinental & Western Air* case, where these statements were made:

“ . . . §406(b) authorizes the Board to fix rates for ‘classes of air carrier.’ It is plain that the uniform rate for the class is an important regulatory device. For §2(d) of the Act, 49 USCA §402, 10A FCA title 49 §402, looks to the sound development of an air transportation system through competition. A uniform rate forces carriers within a given class to compete in securing revenue and in reducing or controlling costs.” (336 U. S. 601, at pp. 606-607.)

The authority to encourage competition through uniform mail rates, which do not necessarily reflect or correspond to the individual carrier’s “need” for compensation, is not different from awarding mail pay to encourage improvement of route structures and betterment of economic conditions in the industry. The public benefit in both uses of the rate-making power is large and self-evident.

It is proper and fitting that the Board be afforded ample flexibility in its rate-making power to permit it to accomplish the broad purposes of the Act, and not alone those purposes specified in Subsection 406(b). The Court of Appeals denied the Board this flexibility.

Conclusion.

The judgment of the Court of Appeals is wrong and should be reversed and the cause remanded to the Board for further proceedings.

Los Angeles, California, November 12, 1953.

Respectfully submitted,

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APPENDIX A.

UNITED STATES COURT OF APPEALS for the District of Columbia Circuit

No. 11259

Arthur E. Sommerfield, Postmaster General of the United States, and The United States of America, on behalf of the Postmaster General, Petitioners, v. Civil Aeronautics Board, Respondent.

No. 11324

Western Air Lines, Inc., Petitioner, v. Civil Aeronautics Board, Respondent.

On Petitions for Review of Orders of the Civil Aeronautics Board. Decided May 4, 1953.

Mr. Daniel M. Friedman, Special Assistant to the Attorney General, Department of Justice, *pro hac vice*, by special leave of Court, with whom *Mr. Newell A. Clapp*, Acting Assistant Attorney General, Department of Justice, was on the brief, for petitioners in No. 11259. *Mr. Charles H. Weston*, Chief, Appellate Section of the Antitrust Division, Department of Justice, and *Mr. William E. Kirk, Jr.*, Assistant United States Attorney at the time of argument, also entered appearances in behalf of the petitioners in No. 11259.

Mr. Hugh W. Darling for petitioner in No. 11324. *Mr. L. Welch Pogue* also entered an appearance in behalf of petitioner in No. 11324.

Mr. O. D. Ozment, Attorney, Civil Aeronautics Board, with whom *Mr. Emory T. Nunneley, Jr.*, General Counsel,

Civil Aeronautics Board, was on the brief, for respondent, *Mr. John H. Wanner*, Associate General Counsel, Civil Aeronautics Board, also entered an appearance in behalf of respondent.

Before PRETTYMAN, PROCTOR and BAZELON, Circuit Judges.

PRETTYMAN, *Circuit Judge*: These cases concern orders of the Civil Aeronautics Board which fixed the compensation of Western Air Lines for the transportation of mail from May, 1944, through December, 1948. The dispute revolves about Section 406 of the Civil Aeronautics Act.¹ The proper treatment of several matters is involved.

Principally the petitions concern the treatment of the profit derived by Western from the sale to United Air Lines of a certificate for an air route and certain equipment used in connection therewith. Prior to September 15, 1947, Western owned a certificate for Route 68—between Los Angeles and Denver. After a hearing the Civil Aeronautics Board approved the sale of the route and the equipment to United Air Lines² for a total price of \$3,750,000. Of this \$722,000³ was then computed as profit on the sale of tangibles and \$447,000 as profit on the sale of intangibles. The Board decided that the transfer of the route at the amount to be paid by United was in the public interest, because the profit on the transaction would provide the necessary incentive for Western

¹52 Stat. 998 (1938), as amended, 49 U. S. C. A. §486.

²United-Western, Acquisition Air Carrier Property, 8 C. A. B. 298 (1947).

³Later recomputed to be \$648,102.

to make a sale and the purchasing carrier could operate the property to greater advantage to the public. The Board acted upon the premise that it has no power to force a carrier against its will to transfer property to another carrier; its only power to influence such transfers is the power of inducement. It decided that a profit on a sale would be such an inducement. Hence it approved the sale.

When the Board came, in the present proceeding, to the determination of compensation to Western for the transportation of mail, a problem arose as to the treatment of this profit in the computations.

The statute, in pertinent part, provides:

“(a) The Board is empowered and directed * * * to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft * * *.

“(b) * * * In determining the rate in each case, the Board shall take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.”⁴

⁴*Supra*, note 1.

The statutory language which is critical in the present dispute is "the need of each such air carrier for compensation * * * sufficient * * *, together with all other revenue of the air carrier, * * * to maintain and continue the development of air transportation."⁵

Perhaps the problem is made clearer by use of a little simple arithmetic. If a carrier has \$1,000,000 in revenue and \$1,300,000 in expenses, obviously it needs \$300,000 to break even; the "break even need." Then it needs a return on its investment and some working capital; let us say \$200,000 for those needs. The statute says that the carrier should receive the amount needed not only to insure the performance of the service but also to enable it to continue the development of air transportation. Let us suppose that for the latter purpose the carrier needs another \$100,000. In sum the carrier needs \$600,000. Now, obviously, in this calculation the greater the amount of the carrier's existing revenues, the less the amount it needs by way of additional mail pay; and the less the revenues the greater the additional mail pay. So the inclusion of a given amount in revenues lessens the mail pay by that amount, and the omission of an amount from revenues increases the needed mail pay. Such is our present problem.

The Board at first decided that the entire profit on the sale of Route 68 was "other revenue," and it included this amount as revenue in calculating the amount of mail pay needed by Western. The effect was to reduce the mail pay by that amount. Upon reconsideration the

⁵Of course the statute provides, in effect, for a minimum which is actual compensation for service performed. That payment is not in dispute here.

Board changed its position. It included the profit from the sale of tangibles as "other revenue" in its calculation, but it did not include the profit from the sale of intangibles. The effect was to reduce mail pay by the amount of the profit on the tangibles, but the profit on the intangibles was left out of the calculation entirely.

The Postmaster General is a party in interest by reason of the duties in respect to mail pay imposed upon him by the statute.⁶ He says the Board was in error in its treatment of the profit on the intangibles. Western says the Board was in error in its treatment of the profit on the tangibles. The Postmaster General would include in revenues the entire profit on the sale of the route and the equipment. Western would exclude the entire profit from revenues in the calculation.

We turn first to the problem of the profit on the tangibles. This was a gain derived from the sale of capital assets. As such it was "income" within the meaning which that term has had ever since *Doyle v. Mitchell Bros. Co.*⁷ But our problem is whether it was "revenue" within the meaning of this rate-making statute. We think the answer should be sought chiefly in the substantive meanings of the statutory provisions rather than in the semantics of the phrases.

The difficulty of the problem arises because this proceeding is to determine a rate of compensation for a past period. Ordinarily, of course, rates are fixed for the future. We think it clear that the profit from an isolated past sale of capital assets could not be included in a

⁶Sec. 406 of the Act, 52 Stat. 998 (1938), 49 U. S. C. A. §486.

⁷247 U. S. 179, 62 L. Ed. 1054, 38 S. Ct. 467 (1918).

calculation of compensation to be paid in future years for carriage of the mail. It would not be anticipated revenue in the future period. With that proposition the Board agrees. In fixing the rate for the future it has considered as revenue only reasonably anticipated items.

Western bases its foremost argument upon the foregoing as a premise. It insists that the present proceeding is a rate-making proceeding and nothing else; that a rate-making proceeding must be, in contemplation of law, rate-making for the future—a prospective rate-making, since, it says, rate-making is inherently a prospective concept. The Board itself has several times so held. And, of course, that is a generally accepted view as to utility rates. There is great power in that argument.

But we are impressed by the practical aspects of the situation. In this instance the Board was in fact looking at a period which had passed. The actual facts as to revenues and expenses for that period were known. The actual need, or lack of it, of the carrier in that period was known. In saying that the Board was looking at a past period we are not departing from the rule in the *T. W. A.* case.⁸ The period began when the petition for the rate-making was filed, *i. e.*, May, 1944; as of that date the rate-making was prospective. When the Board got around to making its findings and decision the period 1944-1948 was past. It is to the latter actually that we refer.

At this point the two different considerations embodied in this statute must be noted. The statute provides for actual compensation for the service performed in carrying

⁸*T. W. A. v. Civil Aeronautics Board*, 336 U. S. 601, 93 L. Ed. 911, 69 S. Ct. 756 (1949).

the mail—a so-called service rate. This is the ordinary purpose of a utility rate. It involves reimbursement for expenses incurred in performing the service, return on the investment used in the service, and a reasonable profit on the transaction. This much is due whether the service is past or future. In the case at bar no dispute arises in respect to that phase of the matter.

But this statute adds to these ordinary features of a utility rate another consideration. It provides that the pay for carrying the mail shall be sufficient to meet the carrier's need. It describes that need as being for funds to perform the service of carrying the mail and also to maintain and develop air transportation. The problem under this provision of the statute is: How much does the carrier need? The answer depends upon (1) the gross, or total, need in dollars and (2) how much the carrier will have outside of mail pay.

In the ordinary case, where the rates are for the future, the revenue of the carrier must be anticipated. But where the pay is being computed for a past period may the Board accept as a fact that which it knows to be a fact, or must it ignore the known fact and compute the rate as though it were looking at the unknown future as of the date of the beginning of the period? The Board knew, and we all know, that Western had in this period this \$1,000,000, or thereabouts, in profit. That profit was derived from the disposition of assets acquired for or created by its operations under its certificate.

Let us suppose, as was the case in the basic findings here, that Western's total non-mail revenue was about \$33,000,000 and its total operating expenses were about \$36,000,000. How much does it need? How much does it

need if, in addition to the \$33,000,000, it also has a special profit of \$1,000,000? Does it actually need \$3,000,000, or does it actually need only \$2,000,000?

The gist of the answer lies in the fact that we are to determine "need." We are not determining merely adequate compensation for services rendered, in the ordinary public utility sense. To be sure, the payment is cast by the statute as a rate, and the process as a rate-making. But even so the Supreme Court held in the *West Ohio Gas* case⁹ that, when the period under consideration has passed, fair and reasonable rates should be ascertained from what is known and not from a *nunc pro tunc* estimate. In the case now before us the disputed basic consideration is a need, a need beyond the requirements of fair compensation for a service performed, not dependent upon the amount or the nature of the service rendered. *A fortiori*, from the *West Ohio Gas* case, the amount of need for a period which has passed must be ascertained in the light of known facts.

It seems to us that under this statute the Board, in fixing a rate of compensation for a past period, may view the facts as it knows the facts to be, that in determining "need" it is not compelled to ignore that which it knows. We conclude that in ascertaining Western's need for the period May, 1944, to December, 1948, the Board was permitted to take into consideration the fact that Western had this profit in that period from the sale of these assets.

We fully realize that our view of the statute will give rise to difficulties in respect to losses and also in respect

⁹*West Ohio Gas Co. v. Comm'n* (No. 2), 294 U. S. 79, 82, 79 L. Ed. 773, 55 S. Ct. 324 (1935).

to unusual or unanticipated earnings. The rule may make too much depend, from the standpoint of the carrier, upon tactical decisions whether and when to file petitions for rate-making. But we think such possibilities cannot negative statutory terms. Moreover other difficulties arise from any other rule. And, again, it seems to us that much of the anticipated difficulty can be prevented by expedition on the part of the Board, so that what is prospective in legal theory will be prospective in actual fact. If expeditious disposition of petitions does not meet the troubles arising from the rule, it is always possible that Congress may change the statutory provision. Our part is done when we conclude what Congress meant by the provision now before us.

We turn next to the treatment of the profit on the intangibles. The Board did not find, and it does not claim now, that Western itself needs the additional amount of mail pay which is shown when the profit on the sale of the intangibles in this transaction is omitted from "other revenue" in the computation. The claim of the Board is that it can allow Western to exclude this sum from stated revenues in order to encourage other carriers (not Western) to follow a given course of action. The Board said, in its opinion in the present case, that it wished to emphasize that the "decision not to include the net profit from the sale of intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers. In other words, we have decided not to offset this profit against the carrier's need because we are seeking in this way to spur the development of a self-sufficient air transport industry."

We recognize the force of the Board's description of the desirability of encouraging carriers to transfer routes and other property. But we cannot find in the statute any power conferred upon the Board to do so in fixing mail pay. We do not find any mail pay provision which is authority for the Board to provide incentives to the industry generally for the development of air transportation through the voluntary actions of carriers.

In the first place, the language of the statute sharply limits development allowances to the needs of the carrier under consideration. (1) The statute speaks of the "need" of the carrier. It does not speak of the desirability of allowances. It does not speak of purely bonus awards. (2) It speaks of "each" air carrier and compensation sufficient to enable "such air carrier" to develop. The statute is not cast in terms applicable to the general field of air transportation but to the situation in which each air carrier finds itself. (3) The statute provides that the mail pay shall be sufficient "to enable" the air carrier to maintain and continue development. This is a sharply limited expression. It does not extend to bonus awards which might be encouraging to the industry generally. Thus we think that, while the so-called "need" provision of the statute, above quoted, does provide for the payments of sums sufficient to enable the carrier under consideration to maintain and continue development of air transportation, such payments are restricted to the need of each individual carrier to maintain and continue a development program of its own.

In the second place, the Supreme Court held in the *T. W. A.* case, *supra*, that the mail pay provisions of this statute describe a rate-making authority, and the Court

said that the statutory language does not suggest that Congress intended to break with the traditions of public utility rate-making. Allowances designed as developmental incentives for the utility whose rates are being determined are quite common in public utility rate-making. But the award of bonus subsidies for the purpose of encouraging an industry generally to follow courses deemed desirable by the regulatory authority is a vast departure from rate-making. Mr. Justice Jackson made the distinction indisputably clear in his dissent in the *T. W. A.* case. He was of the opinion that in these provisions of the statute Congress intended to subsidize the carriers and to underwrite their revenues. We think that the decision in the *T. W. A.* case as to the nature of the mail pay provisions leaves no room for bonus subsidies not connected with the particular carrier's own need. So the statute does not support the theory upon which the Board desires to go in this proceeding in respect to the profit from the intangibles.

We must conclude, therefore, on this point that the Board was in error in the theory upon which it excluded from the calculation the profit from the sales of the intangibles.

The parties dispute the Board's treatment of federal income tax liabilities in its computation of the mail pay. The tax liability upon an estimated basis as of the beginning of the period was some \$600,000. It developed that, due to carry-back losses and other provisions of the federal tax statutes. Western had little or no tax liability for this period. In its final orders on mail pay the Board acted upon the latter basis of fact. We think it was

correct in doing so. The preceding discussion is sufficient as a statement of our reasons.

Western also asserts that the Board erred in including as "other revenue" in the calculation of mail pay the profits derived from the operation of restaurants and slot machine concessions at its airports. We think the Board was clearly correct in this treatment. When the statute says "all other revenue" it must mean to include revenue derived from activities incidental to the operation of the airline. Whether it would also include revenue from activities unconnected with airplane operation is a question not before us and upon which we intimate no opinion.

Western asserts as reversible error the decision of the Board to fix in this proceeding the mail pay beginning in May, 1944. Western says that the consideration should have begun as of January 1, 1946. But the Board has power under the statute (Sec. 406(a)) to "make such rates effective from such date as it shall determine to be proper," and the Supreme Court held in the *T. W. A.* case that that clause empowered the Board to go back as far as the date of the filing of the petition. That is what the Board did in this case. Western filed its petition for redetermination of mail pay on May 1, 1944.

We add one further comment in regard to the expressions "offset," "deduction" and "recapture" used by the parties in describing the treatment of the profit from the sale of the assets if it be included in revenue. The phraseology would not be important if it did not embody

erroneous ideas. The need which this statute contemplates is a net figure; the extra amount which appears necessary over and above that which the carrier has. The process provided by the statute is for an affirmative ascertainment of that need. The need is not a gross figure from which offsets or deductions are made. Thus the passenger revenue etc., is not "offset" against or "deducted" from the need of the carrier. None of the earned revenue is recaptured. The bare, uncomplicated situation is that when the carrier has substantial revenues from non-mail sources the margin of its need for mail pay is less. In practical dollar effect, and perhaps in accounting entries, the treatment may be set up as a gross need with offsetting items, and so it takes on an appearance of recapture. But the legal contemplation of the statute is not that, and the use of the quoted terms leads to erroneous reasoning.

The necessity for reconsiderations, redeterminations and recalculations in the light of this opinion causes us to remand the matter to the Board. The remand is to enable the Board to determine, in the light of this opinion and pursuant to the statutory terms, the amount of compensation to be paid Western for the transportation of mail during the period here involved—May, 1944, to December, 1948.

Affirmed in part, reversed in part, and remanded.

BAZELON, *Circuit Judge*, concurring: I agree with the court's opinion and its comment that the rule we adopt in construing the statute "will give rise to difficulties in respect to losses and also in respect to unusual or unanticipated earnings"¹ but I am unable to agree that "much of the anticipated difficulty can be prevented by expedition on the part of the Board."² I think these difficulties or "other difficulties [which might] arise from any other rule"³ are inherent in the statute and will persist so long as there is no express differentiation therein between compensation for mail service and need payments to subsidize the development of air transportation. This is so because the absence of such a distinction, says the Supreme Court, requires the application of traditional principles of rate making.⁴ The effect of this is to make applicable to subsidy as well as compensation payments the familiar principle that "past excessive earnings belong to the [carrier] just as past losses must be borne by it."⁵ Therein lies the mischief. For that principle derives its validity from the premise that rates are calculated to allow for some financial risk on the part of the public utility.⁶ But since the very purpose of need or subsidy payments is to remove any vestige of risk, that principle has no place in fixing such non-rate payments.

¹Majority opinion, p. 8.

²*Ibid.*

³*Ibid.*

⁴*Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601, 605 (1949).

⁵*Washington Gas Light Co. v. Baker*, 88 U. S. App. D. C. 115, 125, 188 F. 2d 11, 21 (1950), *cert. denied*, 340 U. S. 952 (1951). And see my concurrence this day in *Summerfield, et al. v. Civil Aeronautics Board*, No. 11351.

⁶*Ibid.*, and cases cited in note 15 therein.

APPENDIX B.

RATES FOR TRANSPORTATION OF MAIL

Board to Fix Rates

Sec. 406 [52 Stat. 998, 49 U. S. C. 486] (a) The Board is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith (including the transportation of mail by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same; and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft.

Rate-Making Elements

(b) In fixing and determining fair and reasonable rates of compensation under this section, the Board, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes

of air carriers, and different classes of service. In determining the rate in each case, the Board shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation⁷ of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and (the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense).

Statement of Postmaster General and Carrier

(c) Any petition for the fixing of fair and reasonable rates of compensation under this section shall include a statement of the rate the petitioner believes to be fair and reasonable. The Postmaster General shall introduce as part of the record in all proceedings under this section a comprehensive statement of all service to be required of

⁷So in original.

the air carrier and such other information in his possession as may be deemed by the Board to be material to the inquiry.

Weighing of Mail

(d) The Postmaster General may weigh the mail transported by aircraft and make such computations for statistical and administrative purposes as may be required in the interest of the mail service. The Postmaster General is authorized to employ such clerical and other assistance as may be required in connection with proceedings under this Act. If the Board shall determine that it is necessary or advisable, in order to carry out the provisions of this Act, to have additional and more frequent weighing of the mails, the Postmaster General, upon request of the Board, shall provide therefor in like manner, but such weighing need not be for continuous periods of more than thirty days.

Availability of Appropriations

(e) Except as otherwise provided in section 405(k), the unexpended balances of all appropriations for the transportation of mail by aircraft pursuant to contracts entered into under the Air Mail Act of 1934, as amended, and the unexpended balances of all appropriations available for the transportation of mail by aircraft in Alaska, shall be available, in addition to the purposes stated in such appropriations, for the payment of compensation by the Postmaster General, as provided in this Act for the

transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, between points in the continental United States or between points in Hawaii or in Alaska or between points in the continental United States and points in Canada within one hundred and fifty miles of the international boundary line. Except as otherwise provided in section 405(k), the unexpended balances of all appropriations for the transportation of mail by aircraft pursuant to contracts entered into under the Act of March 8, 1928, as amended, shall be available, in addition to the purposes stated in such appropriations, for payment to be made by the Postmaster General, as provided by this Act, in respect of the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, between points in the United States and points outside thereof, or between points in the continental United States and Territories or possessions of the United States, or between Territories or possessions of the United States.

Payments to Foreign Air Carriers

(f) If any case where air transportation is performed between the United States and any foreign country, both by aircraft owned or operated by one or more air carriers holding a certificate under this title and by aircraft owned or operated by one or more foreign air carriers, the Postmaster General shall not pay to or for the account of any such foreign air carrier a rate of compensation for transporting mail by aircraft between the

United States and such foreign country, which, in his opinion, will result (over such reasonable period as the Postmaster General may determine, taking account of exchange fluctuations and other factors) in such foreign air carrier receiving a higher rate of compensation for transporting such mail than such foreign country pays to air carriers for transporting its mail by aircraft between such foreign country and the United States, or receiving a higher rate of compensation for transporting such mail than a rate determined by the Postmaster General to be comparable to the rate such foreign country pays to air carriers for transporting its mail by aircraft between such foreign country and an intermediate country on the route of such air carrier between such foreign country and the United States.

FEB 15 1954

HAROLD B. WILLEY, Clerk

IN THE
Supreme Court of the United States

Nos. 224 and 225.
October Term, 1953

vs.
CIVIL AERONAUTICS BOARD, *Petitioner,*

ARTHUR E. SUMMERFIELD, Postmaster General of the United States,
THE UNITED STATES OF AMERICA, on Behalf of the Postmaster
General, and WESTERN AIR LINES, INC.

vs.
WESTERN AIR LINES, INC., *Petitioner,*

CIVIL AERONAUTICS BOARD, ARTHUR E. SUMMERFIELD, Post-
master General of the United States, and the UNITED STATES OF
AMERICA, on Behalf of the Postmaster General.

**PETITION OF WESTERN AIR LINES, INC.,
FOR REHEARING.**

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master General of the United States, and the UNITED STATES OF
AMERICA, on Behalf of the Postmaster General.

**PETITION OF WESTERN AIR LINES, INC.,
FOR REHEARING.**

Western Air Lines, Inc., respectfully petitions this
Court to grant a rehearing of its judgment and decision
in these cases delivered on February 1, 1954.

Preface.

This controversy arose out of conflicting interpreta-
tions placed upon Section 406 of the Civil Aeronautics Act
by the two Federal agencies affected and by Western.
This Court has construed the statute in a manner op-
posed to the views of the Federal agency having the duty
of administering the statute.

Important questions in the construction of the statute are involved, and a real need exists for the Court to lay down clear guides for the benefit of the Federal agencies affected and the air transportation industry as a whole. The decision is wanting in definiteness.

The purpose of this petition is to point out the deficiencies in the opinion and the reasons why the decision should be recast.

Reasons for Granting a Hearing.

1. The Opinion Hinges on "Subsidy" Without Statutory Justification.

The idea that a so-called "subsidy" rate of compensation for transporting the mail, as contrasted with what has been styled a "service" rate, is at issue permeates and influences the opinion, although the words "subsidy" and "service" are not in the statute. To the extent that there be an unexpressed difference between rates under the statute, identical words used by the Congress to describe both types of rates should not be given differing contexts depending upon the type of rate in question.

The point is staged by the statement in the opinion that "Some air mail rates are service rates, based on mail-miles flown; others are subsidy rates based on 'need'" (Printed opinion, p. 4). There is no statutory basis for the distinction. Contrary to the Court's statement, "service" as well as "subsidy" rates under the statute are based on "need"—the so-called "service" rate, on "the *need* of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service," and the so-called "subsidy" rate, on "the *need* of each such air carrier for compensation for the trans-

portation of mail sufficient . . . to enable" the air carrier to maintain and continue the development of air transportation. The same word "need" was used by the Congress to introduce two separate factors to guide the Board in fixing fair and reasonable rates under the statute. The same word may not be given dual and different meanings, as suggested by the decision.

2. "Need" Is Not the Sole Criterion for Mail Compensation.

The Court's postulate that the "standard prescribed by Congress . . . is 'the need' of the air carrier whose subsidy rates are being fixed" and that "Western's 'need' is the measure of the amount authorized by Congress" (Printed opinion, p. 6) fails for lack of demonstration. The express language of Section 406(b) makes the "need" of the air carrier one only of the standards prescribed by the Congress for the Civil Aeronautics Board to "take into consideration, among other factors," in determining rates of compensation for carrying the mail. The statute does not bind the Board as to the part its consideration of the rate-making factors should play in its final determination or as to what weight each factor should be given. The decision ignores the statute and binds the Board to look only to the "need" of the air carrier.

3. "Need" Is Not a Limiting Factor.

The Court makes an implied finding that the rate of compensation under the statute may not exceed the particular carrier's "need." There is nothing in the statute justifying the conclusion that the "need" of an air carrier establishes a maximum above which the Board may not go. All the Board is required or able to do

under the statute is to "fix fair and reasonable rates of compensation for the transportation of mail by aircraft." (Section 406(a).) This the Board did.

4. The Board Acted Within Its Discretion.

The opinion contains an erroneous finding that "the Board . . . forsook the standard of 'need' and adopted a different one" (Printed opinion, p. 5). The record is clear. The Board determined and *considered* the compensation "needed" by Western and then, within its discretion, adjusted that compensation by the amount required to encourage voluntary route transfers which would improve the air route pattern of the nation. The Board met its obligations under Sections 2 and 406 of the Act, in the only way possible to effectuate the desires of the Congress.

5. "Need" for Compensation Is Not a Requirement.

The opinion intimates that if the Board had found that there was "need" for the payment of an "additional subsidy" to Western, this might have satisfied the Court's interpretation of the statutory requirement (Printed opinion, p. 6). But the statute does not require the Board to find a "need" for compensation for transporting the mail. As a *guide* the Congress directed the Board to consider, among other things, the "need" of the air carrier for compensation. The Congress did not intend to place the Board under a requisition to act solely on the strength of such "need," in disregard of other pertinent considerations. The mandate of the statute is that the Board shall fix and determine "fair and reasonable rates of compensation for the transportation of mail by aircraft," not that the Board shall fix such rates but only

to the extent of a "need" for compensation. If there be no actual economic "need" for compensation for carrying the mail, because the carrier's treasury is "lush," the Board is not excused from fixing a rate. If so, the statute would be unconstitutional.

6. The Opinion Feigns a Definition of "Revenue."

The imperfect syllogism underpinning the Court's construction of the statutory words "all other revenue" is that because compensation for the transportation of mail is flight income, "all other revenue" must include non-flight income from incidental air carrier activities (Printed opinion, p. 4). The conclusion is a *non-sequitur*, because it is equally reasonable to interpret "other revenue" as limited to the categories of flight and operating income, other than mail revenue, normally generated by air carriers. Gain from the sale of a route and profits from the operation of a slot machine concession are not operating or flight income but rather are sporadic and fortuitous collateral income not susceptible of forecast by the Board.

7. The Opinion Substitutes "Income" for "Revenue."

It is assumed that "all other revenue" includes non-flight income from incidental air carrier activities, but the Court made no attempt to prick out a line between incidental air carrier activities and those air carrier activities, if any, which are not incidental. "Incidental" affords no guide because the word is incapable of abstract meaning.

The announced rule of these cases is that net profits from the operation of a slot machine concession and a gain from the sale of a route stem from incidental air carrier activities and therefore constitute "revenue." If these

items of income be "revenue," it necessarily follows that all income of an air carrier, whatsoever the source, is "revenue" within the meaning of Section 406(b). The only possible justification for the decision is that anything an air carrier does is an incidental air carrier activity, because the actor is an air carrier. Hence, "revenue" really means "income."

The Court has failed to heed a careful choice of words by the Congress, for if the Congress had intended "revenue" to mean "income," it would have said "all other income." Deficiencies in the statute, if such there be, may not be remedied by this Court but must be left for action by the Congress.

8. No Definitive Meaning of "Revenue" Is Reached.

The decision meets none of the contentions advanced by Western with respect to the meaning of the statutory words "all other revenue of the air carrier." That category, however inclusive, may not be broader than the intended meaning of the word "revenue," and if the Congress meant "income" it would have used "income." The Court has not attempted to define "revenue" nor has it ruled that "revenue" means "income." The meaning of the language was left *in vacuo*.

The manifest intent of the Congress in Section 406 of the Civil Aeronautics Act was to establish a scheme for fixing prospective rates of compensation for transporting the mail by aircraft. The Court gave no weight to such intent in construing the statute, although it is apparent that income of the nature of the items here in question could not have been in the minds of the Congress when it chose to use the word "revenue."

Finally, the Court has not met the contention that capital gains may not be used to reduce compensation for transporting the mail because capital losses are not recoverable through such compensation. To paraphrase conversely a statement of the Court, if the carrier's treasury be depleted, "the need" of the carrier increases whether the poverty be due to transportation activities or to activities incidental thereto. But neither the Court nor the Board has suggested that losses from incidental air carrier activities—including, as the Court would have it, the sale of capital assets—may be replenished through mail pay. The fair rule is that the stockholders, who, under our system of non-government owned carriers, must furnish and replace capital assets, shall have the benefit of capital gains. The decision, shattering every concept of justness, confiscates capital gains to the use of the general public at the expense of the stockholders, who must bear the burden of capital losses.

Conclusion.

The uncertainties retained and created by the decision will harass the air transportation industry and provoke further litigation. These are the pleadings for reconsideration.

Though it be the will of the Court to adhere to its first conclusion, the points still puzzling the responsible Federal agencies and the American flag air carriers should be placed in focus. If "all other revenue" in fact means "all other income, regardless of source" because the inclusive nature of the category precludes a narrow reading, the Federal agencies and the industry should be so advised with preciseness and not be compelled to guess.

If it means less than that, clear specifications should be written for the term "income from incidental air carrier activities." And those concerned should be told whether losses from incidental air carrier activities are to be recouped or only the profits siphoned over.

Los Angeles, California, February 12, 1954.

Respectfully submitted,

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Certificate of Counsel.

I certify that the foregoing petition for rehearing is presented in good faith and not for delay.

Los Angeles, California, February 12, 1954.

HUGH W. DARLING,
*Attorney for Petitioner,
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for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." ² The controversy in the present cases turns on the meaning of the

by an air carrier by other means than aircraft whenever such transportation is incidental to the transportation of mail by aircraft or is made necessary by conditions of emergency arising from aircraft operation), by each holder of a certificate authorizing the transportation of mail by aircraft, and to make such rates effective from such date as it shall determine to be proper; (2) to prescribe the method or methods, by aircraft-mile, pound-mile, weight, space, or any combination thereof, or otherwise, for ascertaining such rates of compensation for each air carrier or class of air carriers; and (3) to publish the same; and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft."

² "In fixing and determining fair and reasonable rates of compensation under this section, the [Board], considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

words "the need of each such air carrier" and "all other revenue of the air carrier."

Western Air Lines filed a petition for a rate order April 26, 1944. In 1951 the Board finally determined the rate applicable between May 1, 1944, and December 31, 1948. During this open-rate period Western realized some \$88,000 in profits from the operation of restaurants and other concessions at airport terminals. The Board determined that this income was "other revenue" available to reduce mail pay. During the open-rate period Western with approval of the Board³ sold to United Air Lines its certificate and properties for air operations (Route 68) between Los Angeles and Denver, at a profit in excess of \$1,000,000. The Board treated the profit derived from the sale of the tangible assets (approximately \$650,000) as "other revenue" and reduced the mail compensation by that amount. But it declined to reduce the mail pay allowance by the profit realized from the sale of the "intangible value" of the route. The Board concluded that that amount should not be used in offset because it wanted "to encourage improvement of the air route pattern through voluntary route transfers by other air carriers." — C. A. B. —.

On review Western challenged the inclusion in "other revenue" of the amounts received from the concessions and the profit from the sale of the tangible assets. The Postmaster General⁴ challenged the exclusion from the offsets of the profit Western made on the sale of the intan-

³ *United-Western, Acquisition of Air Carrier Property*, 8 C. A. B. 298 (1947).

⁴ The Postmaster General has not only the duty to pay the mail rates from appropriations for the transportation of mail by aircraft but also is given standing by § 406 (a) to petition the Board to fix and determine the rates. A change in the function of the Postmaster General was made by Reorganization Plan No. 10 of 1953, effective October 1, 1953, 67 Stat. 644.

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gibles. The Court of Appeals sustained the Board in Western's petition and reversed it in the other petition and remanded the case to the Board for the fixing of a new rate after deducting the entire profit from the sale of Western's Route 68. See 207 F. 2d 200.

Some air mail rates are service rates, based on mail-miles flown; ⁵ others are subsidy rates based on "need." We are here concerned with a subsidy rate which in Western's case was fixed so as to produce a 7 percent return on investment after taxes for the period in question. In other words, the end problem concerns not the amount of money provided for operation and development but the amount of profit over and above all such sums.

We read the Act as meaning that "the need" of the carrier which Congress has directed the Board to consider in fixing a subsidy rate is "the need" of the carrier as a whole. The need specified in § 406 (b) is measured by "compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable" it to develop air transportation, etc. The "compensation for the transportation of mail" is flight income. It seems too clear for argument that "all other revenue" would include nonflight income from incidental air carrier activities. We have found nothing persuasive as indicating that "all other revenue" means transportation revenue. The inclusive nature of the category precludes a narrow reading. If the carrier's treasury is lush, "the need" for subsidy decreases whether the opulence is due to transportation activities or to activities incidental thereto.

By the same reasoning the profit made by Western on the sale of Route 68 is also "other revenue" within the

⁵ See, for example, *Eastern Air Lines, Mail Rates*, 3 C. A. B. 733 (1942).

meaning of § 406 (b). The Board agrees; but it goes on to say that that is not the end of the matter, since the reduction of the subsidy by the entire amount of the profit is not mandatory. The Act, it is true, merely says that the Board in determining the rate "shall take into consideration" various factors, including "the need" of the carrier (§ 406 (b)); and the "need," as we have noted, is not merely for compensation to insure the transportation of mail but compensation for "the development of air transportation" under the prescribed standards. By that standard the "need" in a given case may be so great that profits from other transactions should be allowed in addition to the normal rate. Or, on the other hand, the total revenues of the carrier as against its operating costs and developmental program may be so great that "the need" for subsidy disappears and the carrier is transferred to the service rate for mail pay. The difficulty here is that the Board, in concluding that a part of the profits from the sale to United should not be used as an offset, forsook the standard of "need" and adopted a different one. The Board wanted "to safeguard the incentive for voluntary route transfers." It thought it could not keep this incentive alive in the industry unless the profit were allowed in addition to the subsidy. The Board thought it important to keep that incentive alive in order to promote route transfers and mergers which the Board could not compel. The Board therefore argues that allowance of the profit over and above a subsidy enables Western "to maintain and continue the development of air transportation" within the meaning of § 406 (b), since the sale of Route 68 was consistent with the development program which the Board deemed desirable.

The Act, however, speaks of "the need" of the carrier for the subsidy, not the effect of a policy on carriers in general. This is not a case of recapture of earnings.

Western keeps the entire amount of the profit. The issue is how much additional money Western is to receive in the form of a subsidy. Western's "need" is the measure of the amount authorized by Congress. No finding was made that there was "need" for the additional subsidy, in the sense that otherwise Western would not have been willing or able to make the transfer of Route 68 in accordance with the development program which the Board deems advisable. Whether such a finding would have satisfied the statutory requirement is a question we do not reach, since the opinion of the Board makes plain that other considerations were controlling:

" . . . our decision not to include the net profit from the sale of intangibles was reached solely because we are thus seeking to encourage improvement of the air route pattern through voluntary route transfers by other air carriers." — C. A. B. —.

The standard prescribed by Congress, however, is "the need" of the air carrier whose subsidy rates are being fixed.

Affirmed.

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